Portraits of Leadership

2006 ANNUAL REPORT

ONE-YEAR PERFORMANCE

Years ended September 30 *Dollars in millions, except per share amounts*	2005	2006	PERCENT CHANGE
Sales	$17,305	$20,133	16.3%
Earnings per share	$ 3.40	$ 4.48	31.8%
Dividends per share	$ 1.66	$ 1.78	7.2%
Operating cash flow	$ 2,187	$ 2,512	14.9%
Return on total capital	15.5%	18.4%	
Return on equity	19.4%	23.7%	

FIVE-YEAR PERFORMANCE

Years ended September 30 *Dollars in millions, except per share amounts*	2001	2006	FIVE-YEAR CAGR
Sales	$15,311	$20,133	5.6%
Earnings per share	$ 2.40	$ 4.48	13.3%
Dividends per share	$ 1.53	$ 1.78	3.1%
Operating cash flow	$ 1,708	$ 2,512	8.0%
Return on total capital	11.5%	18.4%	
Return on equity	16.5%	23.7%	

1956

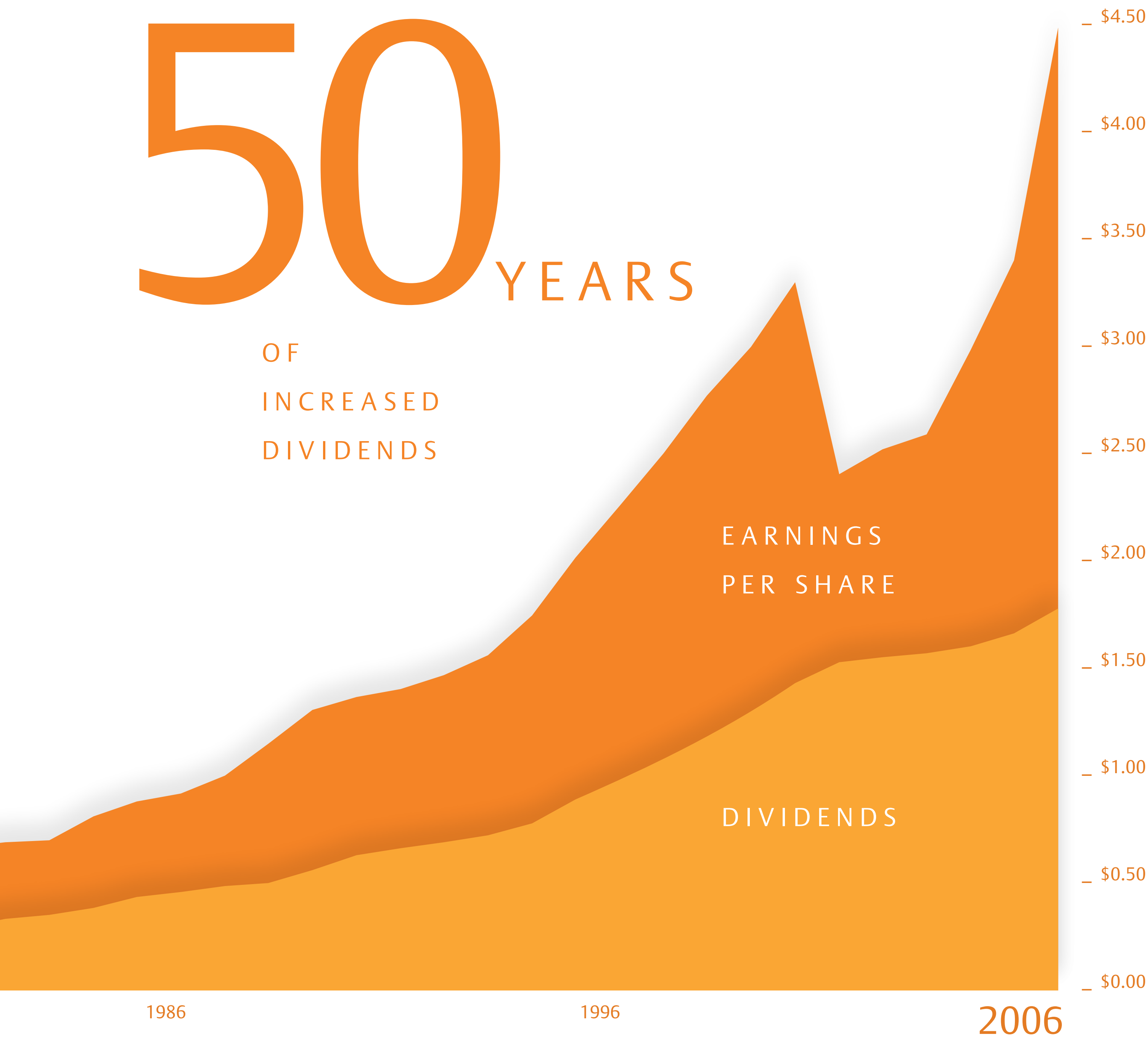
1966

1976

DEAR SHAREHOLDERS,

In 2006, Emerson once again obtained its financial and operating objectives and delivered record levels of sales, earnings per share, and operating cash flow. Dividends increased for the 50th consecutive year, and revenues topped $20 billion, making 2006 a year of significant milestones. Over the last 50 years and especially over the past two decades, Emerson has established a solid reputation as a strong global company ready to face current and future challenges.

Continual strong performance doesn't come by accident. Dedicated, enthusiastic, and creative Emerson leaders throughout the company apply our management process to help meet and exceed operational objectives. This strategic process allows us to address global opportunities and continue to invest in next-generation innovation and technologies to the benefit of shareholders, customers, and employees.



2002 earnings per share is before the $2.23 per share charge from the cumulative effect of a change in accounting principle.

2006 Financial and Operating Highlights

Net sales were a record $20.1 billion, up 16.3 percent from $17.3 billion in 2005. The increase was driven by strong underlying sales growth of 12.5 percent (which excludes the impact of acquisitions, divestitures, and foreign currency translation), well above the long-term target of achieving 5 to 7 percent average underlying growth through the business cycles. Emerson's performance this year reflects a strong industrial economy and continued execution of our eight key growth initiatives.

Earnings per share (EPS) of $4.48 also represented a new record and was an increase of 32 percent from the $3.40 reported in 2005. This performance is substantially better than Emerson's compound annual EPS growth rate of 10 percent over the last 50 years. Strong sales growth and continued focus on operational excellence programs were key to this year's EPS performance.

[FROM LEFT TO RIGHT]

EDWARD L. MONSER
CHIEF OPERATING OFFICER

DAVID N. FARR
CHAIRMAN, CHIEF EXECUTIVE OFFICER, AND PRESIDENT

WALTER J. GALVIN
SENIOR EXECUTIVE VICE PRESIDENT AND CHIEF FINANCIAL OFFICER

CHARLES A. PETERS
SENIOR EXECUTIVE VICE PRESIDENT

"EMERSON HAS ESTABLISHED A SOLID REPUTATION AS A STRONG GLOBAL COMPANY READY TO FACE CURRENT AND FUTURE CHALLENGES."

DAVID N. FARR

Emerson's Tradition
OF PERFORMANCE LEADERSHIP

Return on total capital (ROTC) is a key metric for Emerson, one that directly measures a corporation's ability to earn acceptable returns for shareholders. The goal was an 18 percent ROTC by fiscal 2008, and we are pleased to report that it was achieved during 2006. The combination of strong earnings growth and a focus on the capital needs of the businesses allowed the company to achieve a ROTC in 2006 of 18.4 percent compared with 15.5 percent in 2005. We are proud of this accomplishment and the value creation it signifies for shareholders.

Generating significant cash flow continues to be a key priority for Emerson. A continued focus on cash flow allows Emerson to invest in existing businesses, fund the acquisition of new businesses and technologies, and return appropriate amounts of cash to shareholders. All of these transactions play a role in creating long-term value. The 2006 score card for cash management is good, with operating cash flow of $2.5 billion, an increase of 15 percent from $2.2 billion in 2005. The key uses of this cash were:

- $730 million for dividends, or $1.78 per share. This year represents the 50th consecutive year of dividend increases, a significant milestone for Emerson.
- $862 million for share repurchases. When combined with dividends, this means that Emerson returned 63 percent of operating cash flow to shareholders, slightly exceeding our target of 50 percent to 60 percent.
- $752 million for acquisitions. These investments are key to maintaining a healthy portfolio of businesses capable of delivering acceptable growth and returns over the long term. In 2006, Emerson purchased a number of solid companies across the Network Power, Industrial Automation, and Process Management segments.

Our vision provides

INSIGHT ABOUT WHAT'S AHEAD.

The Leadership That Sets Emerson Apart

At Emerson, our deliberate planning process not only allows productive and efficient operation but also lets us look ahead at the trends that will most impact the global economy and provide the greatest growth potential.

That might sound easy, but it isn't. Some companies claim they can do it, but only a few can. Our long-standing ability to plan, execute, and consistently deliver results with integrity sets Emerson apart.

This leadership, strategic vision, and planning have helped us identify important global issues early, so we could plan for them and build the businesses around the opportunities they create. Today, Emerson is well-positioned to help customers address issues such as:

Energy efficiency,which becomes more important than ever, as energy costs continue to rise and as fuel and power become more expensive.

Our **resources for the world,** which are challenged as never before by a global population that continues to grow and mature.

The **communications revolution,** as driven by an increasing demand for voice and data bandwidth around the world and the need to keep these systems up and running every minute of every day.

Business without borders,as our world shrinks a bit more every day.

Anticipation of these trends is central to what Emerson does. In fact, you may have seen them in the first-ever television commercials Emerson aired this year as part of our global branding campaign that showcased the solutions available to customers around the world.

Emerson's success with these solutions comes from a collaborative team spirit that flows throughout the organization and is fueled and fostered by strong leaders. The following executives of each business platform exemplify this leadership:

- John Berra, who heads Emerson Process Management, is leading the charge to bring a revolutionary wireless communications system to the process industries that will also be used across several other Emerson businesses.
- Pat Sly, of Emerson's Tools and Storage businesses, is overseeing the creation of a $1 billion storage business that continues to push into new markets and develop new technologies while outperforming the competition.
- Tom Bettcher and his Emerson Climate Technologies team are developing an important new heat pump using industry-leading scroll technology while creating an electronics core for the next generation of products and services.
- Ed Feeney, Bob Bauer, and Jay Geldmacher continue to demonstrate that reliable power is a strong core competency by providing innovative Emerson Network Power solutions to telecom, data center, and other mission-critical businesses.
- Jean-Paul Montupet and the Emerson Industrial Automation team are working closely with major manufacturing companies and industry groups to develop customized solutions that drive quality and enhance productivity, all at the best cost.
- Jim Lindemann, of Emerson Appliance Solutions, is helping create unique applications for their technologies and partnering with the gas water-heater industry to improve the safety and performance of these common appliances.

Dollars in billions | *Net sales as originally reported in the company's annual reports.*

Together, this group of leaders is forging the path for Emerson. They are developing new technologies and solutions that are *Forward Thinking*. They're tapping into skills and experience around the world to offer customers the benefit of our *Global Focus*. They're demonstrating our *Sustained Innovation*. And all the while, they're working closely with customers to demonstrate a solid record of *Customer Results*.

These are the essentials of Emerson's success — identifying new opportunities and powering our businesses with the best people and resources so that Emerson is in a position to win.

Emerson's success and strength are much deeper than just these business leaders. They will be the first to tell you that people throughout their organizations are great leaders with significant expertise in their industries. The stories on the following pages give us a glimpse into their worlds.

It is extremely important to Emerson that we maintain the reputation of a highly ethical company. Maintaining that reputation is critical to our success, and we continually communicate the highest ethical standards to employees around the world. Customers and investors alike tell us they value this integrity, and we will continue to reinforce Emerson's commitment to ethical behavior in every day-to-day activity.

Emerson has seen much change over its history, and more change is inevitable going forward. Winning companies see the change coming, accept it, understand it, and make it work for them. We're especially proud of our many recent accomplishments and look forward to the many opportunities ahead.

We thank our shareholders and board of directors for their support, and in particular, we want to welcome Randall Stephenson, chief operating officer of AT&T, to our board. Randall's strong experience in finance, operations, and one of the most complex acquisitions in recent corporate history will be a valuable asset to Emerson.

David N. Farr
Chairman, Chief Executive Officer, and President

Charles A. Peters
Senior Executive Vice President

Walter J. Galvin
Senior Executive Vice President and Chief Financial Officer

Edward L. Monser
Chief Operating Officer

PAT SLY [LEFT]
EMERSON TOOLS AND STORAGE

JOHN BERRA [RIGHT]
EMERSON PROCESS MANAGEMENT

“OVERALL, EMERSON PROCESS MANAGEMENT IS MEETING THE DEMANDS OF THE ENERGY WORLD WITH BETTER QUALITY, EXPANDED CAPACITY, AND IMPROVED EFFICIENCY AND SAFETY.”

JOHN BERRA

Forward Thinking

AND PERCEPTIVE PLANNING

Emerson has always prided itself in developing forward-thinking technologies to help customers stay ahead of the curve, whether in immediate response to their needs or as a result of ongoing research and development programs that look farther ahead.

One of the biggest innovations to come out of Emerson is the wireless technology for the process industries from Emerson Process Management, led by John Berra. A far cry from the wireless Internet access commonly found in coffee shops and public libraries, this wireless technology was developed specifically for the challenging world of refineries, power plants, and other large-scale industrial operations.

The first and largest challenge Emerson engineers needed to overcome was how to deliver a wireless signal within the “canyons of metal,” where ordinary wireless technology is useless. We overcame that challenge by converging the technologies of self-organizing networks, multiple pathways, and “channel hopping” to deliver a consistent, reliable, and robust network.

The biggest benefit for customers comes from more cost-effective installation of sensors. The dramatically lower costs of wireless installation enable operators and engineers to gather more and richer information from around the facility and to use that data with Emerson control systems to increase field intelligence and improve plant efficiency.

Looking ahead, we see that this technology will have a significant impact on both new and existing facilities, reducing installation costs by as much as 90 percent. This technology will allow plant operators to roam the plant with a portable or hand-held computer, carrying all the data they’d normally access only from the control room.

Overall, Emerson Process Management is meeting the demands of the energy world with better quality, expanded capacity, and improved efficiency and safety.

Emerson Storage Solutions, led by Pat Sly, has applied innovative engineering expertise in a similar way, identifying where new technologies and customer needs intersect in the health care industry.

BY THE YEAR 2030
PRODUCTION OF OIL
MUST INCREASE BY
38 MILLION
BARRELS PER DAY TO
MEET THE DEMAND.

We're leading the way

BY DEVELOPING NEW TECHNOLOGIES.

For instance, the InterMetro division, which supplies commercial, food service, and health care storage solutions, identified an industry trend in the convergence of information technology with traditional mobile storage products for improved patient care, safety, and record-keeping. The company seized an opportunity to strengthen its position with the acquisition in 2006 of Flo Healthcare Solutions.

The result is an entry into the fast-growing market segment for new computerized mobile workstations that integrate wireless technologies into a new platform for reliable administration of medications and improved record-keeping. Nurses can wheel workstations directly to the patient's bedside, access medical records over a secure network, and then see the most accurate and up-to-date prescription list for that patient. Nurses can then scan the patient's identification and the prescribed medications to make certain that the patient gets exactly what the doctor ordered.

The workstation then communicates wirelessly with the main hospital systems, updating the patient's records to help ensure a safe and secure procedure.

Closer to most people's homes, Emerson's In-Sink-Erator business has also been looking ahead to the needs of homeowners, especially with its garbage disposer business. Using extensive consumer research, Emerson identified segments of end-users based on their needs and wants for disposer units. Some consumers wanted additional grinding capability, for example, while others wanted a significantly quieter appliance.

The revolutionary solution is the Evolution Series™ household disposers, available in five models to meet the needs of each of these segments. Launched in 2006, the new disposers are fundamentally changing the way homeowners and contractors look at this "fifth kitchen appliance."

How does Emerson prepare for the future? As leaders in our industries, we look ahead with our customers and together identify what their customers will need and where technology is heading. Our experience and expertise help us engineer the forward-thinking solutions that ensure satisfied customers.

TOM BETTCHER
EMERSON CLIMATE TECHNOLOGIES

“WITH OUR GLOBAL FOOTPRINT, WE HAVE SUCCESSFULLY ADAPTED TECHNOLOGIES THAT WERE DEVELOPED FOR ONE REGION IN ORDER TO MEET EMERGING NEEDS IN OTHER REGIONS.”

TOM BETTCHER

Global Focus

AND THOUGHT LEADERSHIP

As the global marketplace expands and changes, Emerson, in cooperation with customers and suppliers, must break down the borders to business. By doing this, Emerson is able to leverage technology used in one part of the world in several other areas and capitalize on growth opportunities.

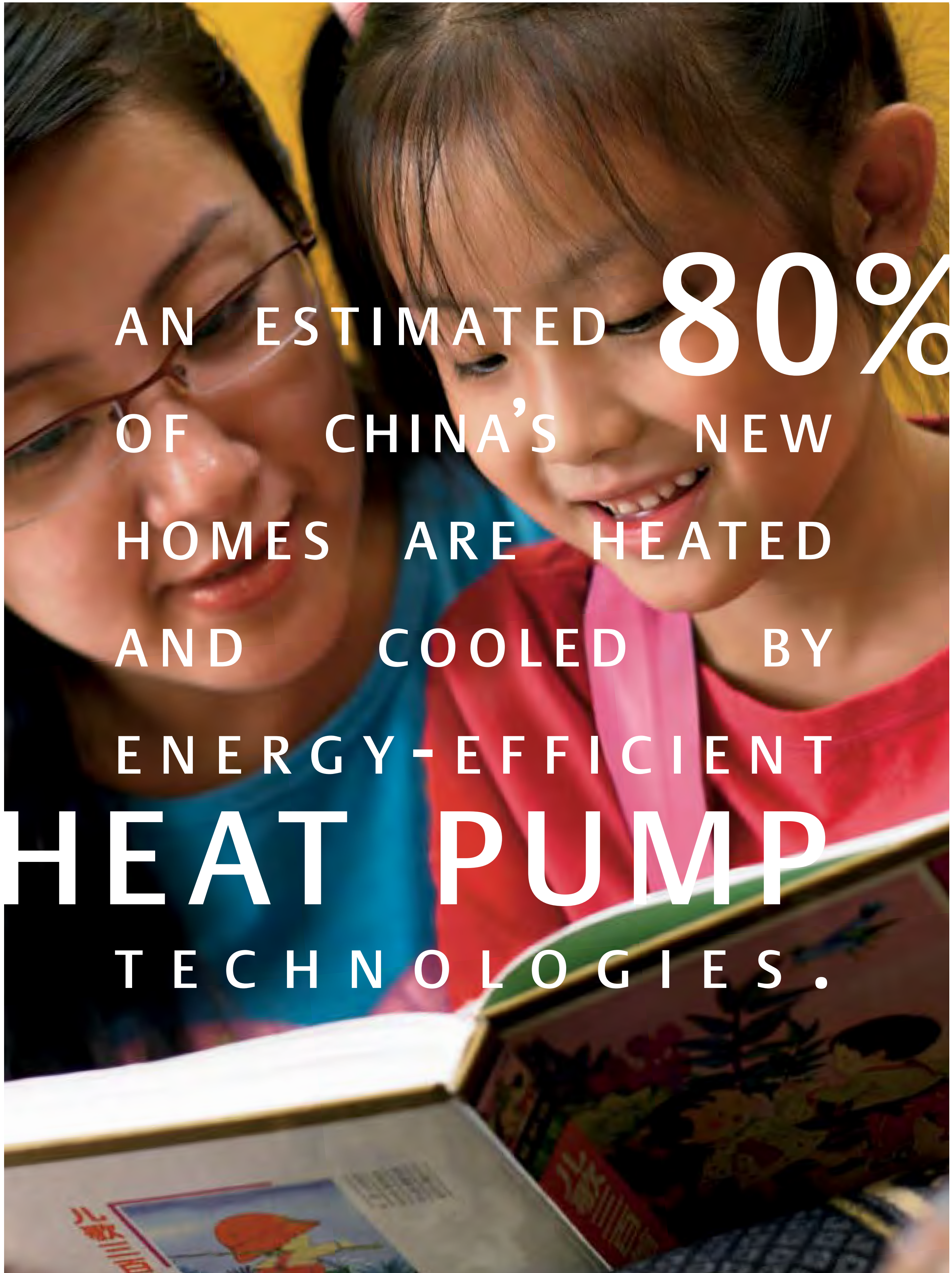
For example, Emerson Climate Technologies, under the leadership of Tom Bettcher, has adapted Emerson’s scroll technology for use in transport refrigeration, residential heating and cooling, and commercial air-conditioning applications.

While heat pumps have been used in the United States for more than three decades, they have been typically well-suited for milder climates. Like an air conditioner in reverse, these heat pumps can effectively transfer heat from outside to inside. Systems using the latest Emerson scroll technology offer significant gains in efficiency and heating performance, allowing the units to be used in the cooler climates of northern Europe and China.

Much of this work has been done in the new engineering center in Suzhou, China. More than 160 engineers, representing seven different Emerson operating units, are working here to add value to our customers and products through our global industry expertise.

We are now adapting this new heat pump scroll technology for the European market, where many homes use hot-water radiators for heat, which are connected to a steam boiler that is fired by gas or oil. Replacing the boiler with a high-efficiency heat pump, which can be powered by renewable energy sources like water, wind, and solar, requires additional technologies now available from Emerson.

Although local requirements vary around the world, Emerson’s global vision and expertise are delivering technologies that



AN ESTIMATED 80% OF CHINA'S NEW HOMES ARE HEATED AND COOLED BY ENERGY-EFFICIENT HEAT PUMP TECHNOLOGIES.

We are there

BOTH GLOBALLY AND LOCALLY.

address these and other common needs. As people around the world are becoming increasingly concerned with their individual energy usage and its impact on the environment, Emerson is working to help countries like China improve overall efficiency standards and consume less power.

In other Emerson Climate Technologies businesses, we're working to make sensors and equipment more reliable by adding electronics for diagnostics to improve efficiency and reduce system maintenance costs. Much like our "smart" valves used in the process industries, these components anticipate problems and alert the operator that part of the system requires attention.

Many of these components are available in our Intelligent Store™ solution. This Emerson solution, with a global focus, is used by some of the largest convenience and grocery store chains in North America and Europe and is emerging in Asia. Intelligent Store technologies allow retailers to remotely monitor and control energy consumption, comfort levels, equipment maintenance, and even food quality. The suite of products provides maintenance, energy, and reliability gains for owners and operators.

Emerson's global reach is in itself a big factor in our success around the world. With our global footprint, we have successfully adapted technologies that were developed for one region in order to meet emerging needs in other regions. In this way, Emerson truly takes a world view to conducting business without borders.

"COMPANIES THAT SEE THE RISKS OF BEING UNPROTECTED ARE TURNING TO EMERSON NETWORK POWER FOR BUSINESS-CRITICAL CONTINUITY SOLUTIONS TO STAY UP AND RUNNING, SHOULD THE UNTHINKABLE OCCUR."

BOB BAUER

Sustained Innovation

AND CUSTOMER COLLABORATION

While many companies develop new technologies, few can create an environment where those new technologies can be built into ongoing, sustainable product lines that stand the test of time. That's exactly what Emerson Network Power is doing under the leadership of Ed Feeney, Bob Bauer, and Jay Geldmacher.

For example, Emerson Network Power works hand in hand with many customers to develop embedded power supplies for a broad range of electronic equipment. Together, these teams develop solutions for the unique requirements of end-users by applying new technologies and solutions.

These customers want smaller, more-powerful power supplies, which requires new topologies and new ways to dissipate heat. And with an eye toward higher efficiency, we're striving to reduce power consumption to better meet new government legislation and customer demands.

Data centers are particularly vulnerable to the excessive heat generated by large server and storage systems. To address this, Emerson Network Power technologies deliver the precision cooling and backup power systems used in these critical data centers, where hundreds of servers and storage systems access trillions of megabytes of information. As these data centers continue to evolve and as centralized computing re-emerges on the scene, Emerson technologies will continue to keep pace.

The benefits of this return to centralized computing are numerous. IT staff can reduce operating costs by running fewer data centers more efficiently while exercising better control of the applications that users require. This can improve security, better protecting the data and avoiding attacks. In a single controllable environment, the IT staff can securely maintain this critical infrastructure and maximize server availability for users around the world.

All of this requires higher levels of clean, reliable power, and efficient cooling systems, both offered by Emerson Network Power.

BOB BAUER [LEFT]
EMERSON NETWORK POWER

JAY GELDMACHER [MIDDLE]
EMERSON NETWORK POWER

ED FEENEY [RIGHT]
EMERSON NETWORK POWER

IN THE NEXT 2 YEARS
THERE WILL BE OVER
1 BILLION NEW
VOICE AND DATA
COMMUNICATORS.

We're ready

WITH NEW SERVICES AND SOLUTIONS.

Today's data centers are also in a state of constant change. New equipment is being installed to replace old equipment almost daily. High-density computing has led to high heat density loads, creating unique combinations of traditional cooling needs and hot spots that require more-advanced solutions. Emerson Network Power stands at the leading edge of this challenge with our stability and endurance to keep pace with technology.

Additionally, Emerson Network Power works to eliminate heat at the source and enable high-density computing in a way that will reduce operating costs. The 2006 acquisition of Knürr has become even more critical, as users seek out unique solutions to package power and cooling technologies in the rack enclosures that house critical equipment.

While centralized computing has become the trend with large businesses, medium-sized and small companies are often less-prepared to deal with natural or man-made disasters that can disrupt their business. Companies that see the risks of being unprotected are turning to Emerson Network Power for business-critical continuity solutions to stay up and running, should the unthinkable occur.

The telecommunications landscape is changing rapidly all over the world. Developing countries are leapfrogging traditional technologies and installing latest-generation communications networks. And they're looking to Emerson to power the networks that will deliver a variety of different services to new customers. In the more-developed world, new technologies, like Voice over Internet Protocol (VoIP) and Internet Protocol Television (IPTV), are creating unique new challenges for both power and cooling.

How does Emerson sustain innovation? At our heart, we're an engineering organization. Emerson engineers understand a wide variety of global applications and know how these applications need to keep pace with technology. As the playing field changes, Emerson continues to deliver unique leading-edge solutions to our customers.

"BY KEEPING AN EYE ON THE FUTURE AND LISTENING TO OUR CUSTOMERS, EMERSON CONTINUES TO UTILIZE TECHNOLOGY AND SYSTEM SOLUTIONS TO MEET THEIR NEEDS."

JIM LINDEMANN

Customer Results

AND PROVEN PARTNERSHIPS

Emerson has a solid track record of providing results for our customers. We continually work closely with them to overcome and solve specific problems. Over the years, the languages, locations, and issues may have changed, but the solutions are still found by listening and learning together.

Examples can be seen throughout the company, especially in Emerson Industrial Automation, led by Jean-Paul Montupet; and Emerson Appliance Solutions, led by Jim Lindemann.

Emerson Industrial Automation, for example, worked closely with Ingersoll-Rand to develop a unique variable-speed motor for the company's air compressors, commonly used in industrial plants to power pneumatic machinery. Since industrial air compressors typically use up to one-tenth of the energy in a facility, a more-efficient compressor would yield significant savings potential.

The energy-reducing features of the resulting Emerson hybrid permanent magnet motor enable Ingersoll-Rand Nirvana air compressors to operate with at least 22 percent less energy than fixed-speed air compressors with conventional induction motors.

Another example of a compelling and urgent customer need comes from Emerson Appliance Solutions, where a group of gas water-heater manufacturers turned to when they needed help.

The gas water-heater industry wanted to enhance the safety of its products, but no viable solution existed. Emerson Appliance Solutions heard the call and responded with the industry's first flammable vapor sensor, which is designed to shut down the system when it detects volatile compounds in the air.

Throughout the development process, Emerson worked in true partnership with the industry to define the issue and to help ensure successful product installation, use, and reliability. Emerson Appliance Solutions listened to our customers and the industry to develop and deliver a truly pioneering solution.

JIM LINDEMANN [LEFT]
EMERSON APPLIANCE SOLUTIONS

JEAN-PAUL MONTUPET [RIGHT]
EMERSON INDUSTRIAL AUTOMATION

BY THE YEAR 2030
THE WORLD'S POWER
DEMANDS WILL GROW
STEADILY TO NEARLY
200% OF CURRENT
GLOBAL CAPACITY.

We’re helping

BY PARTNERING WITH THE BEST.

Similarly, when Little Swan, an appliance manufacturer in China, began developing a high-end washing machine, it needed motor and control expertise. Emerson Appliance Solutions was there with the technology, products, and manufacturing capability to deliver a complete system solution.

Working closely with Little Swan, Emerson provided the necessary technology advantage, and our strong presence in China enabled both companies to develop joint teams, such as design engineering and product introduction. Little Swan needed a solutions-focused partner, and Emerson delivered.

All of these solutions derive from Emerson’s deep knowledge of the industries we serve and of the end-users within those industries. Emerson offers customers combined industry knowledge stemming from global experience to value-added partnerships.

Emerson industry leadership runs deep in each of our business units. Teams of people with different areas of responsibility, for example, engineering, marketing, and sales, share their experiences so that when a solution is developed for one place, we can share it with the world.

In fact, Emerson has specific teams that meet regularly to track technologies and solutions across different product lines. This has improved the ability to actively share and communicate the customer results we develop.

At the end of the day, Emerson’s success depends on how we take our strengths of *Forward Thinking, Global Focus, Sustained Innovation,* and *Customer Results* and apply them to the challenges the world faces. By keeping an eye on the future and listening to our customers, Emerson continues to utilize technology and system solutions to meet their needs.

Financial Review

Report of Management

The Company's management is responsible for the integrity and accuracy of the financial statements. Management believes that the financial statements for the three years ended September 30, 2006, have been prepared in conformity with U.S. generally accepted accounting principles appropriate in the circumstances. In preparing the financial statements, management makes informed judgments and estimates where necessary to reflect the expected effects of events and transactions that have not been completed. The Company's disclosure controls and procedures ensure that material information required to be disclosed is recorded, processed, summarized and communicated to management and reported within the required time periods.

In meeting its responsibility for the reliability of the financial statements, management relies on a system of internal accounting control. This system is designed to provide reasonable assurance that assets are safeguarded and transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with U.S. generally accepted accounting principles. The design of this system recognizes that errors or irregularities may occur and that estimates and judgments are required to assess the relative cost and expected benefits of the controls. Management believes that the Company's accounting controls provide reasonable assurance that errors or irregularities that could be material to the financial statements are prevented or would be detected within a timely period.

The Audit Committee of the Board of Directors, which is composed solely of independent Directors, is responsible for overseeing the Company's financial reporting process. The Audit Committee meets with management and the internal auditors periodically to review the work of each and to monitor the discharge by each of its responsibilities. The Audit Committee also meets periodically with the independent auditors who have free access to the Audit Committee and the Board of Directors to discuss the quality and acceptability of the Company's financial reporting, internal controls, as well as non-audit-related services.

The independent auditors are engaged to express an opinion on the Company's consolidated financial statements and on the Company's internal control over financial reporting. Their opinions are based on procedures which they believe to be sufficient to provide reasonable assurance that the financial statements contain no material errors and that the Company's internal controls are effective.

Management's Report on Internal Control over Financial Reporting

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting for the Company. With the participation of the Chief Executive Officer and the Chief Financial Officer, management conducted an evaluation of the effectiveness of internal control over financial reporting based on the framework and the criteria established in *Internal Control – Integrated Framework*, issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, management has concluded that internal control over financial reporting was effective as of September 30, 2006.

The Company's auditor, KPMG LLP, an independent registered public accounting firm, has issued an audit report on management's assessment of internal control over financial reporting.

David N. Farr

Chairman of the Board, Chief Executive Officer, and President

Walter J. Galvin

Senior Executive Vice President and Chief Financial Officer

Results of Operations

Years ended September 30 | Dollars in millions, except per share amounts

	2004	2005	**2006**	CHANGE '04 - '05	**CHANGE '05 - '06**
Net sales	$15,615	17,305	**20,133**	11%	**16%**
Gross profit	$ 5,566	6,183	**7,168**	11%	**16%**
Percent of sales	*35.6%*	*35.7%*	***35.6%***		
SG&A	$ 3,281	3,595	**4,099**		
Percent of sales	*21.0%*	*20.7%*	***20.4%***		
Other deductions, net	$ 223	230	**178**		
Interest expense, net	$ 210	209	**207**		
Earnings before income taxes	$ 1,852	2,149	**2,684**	16%	**25%**
Net earnings	$ 1,257	1,422	**1,845**	13%	**30%**
Percent of sales	*8.1%*	*8.2%*	***9.2%***		
Earnings per share	$ 2.98	3.40	**4.48**	14%	**32%**

Net earnings and earnings per share for 2005 include a $63 million tax expense ($0.15 per share) for repatriation under the American Jobs Creation Act.

OVERVIEW

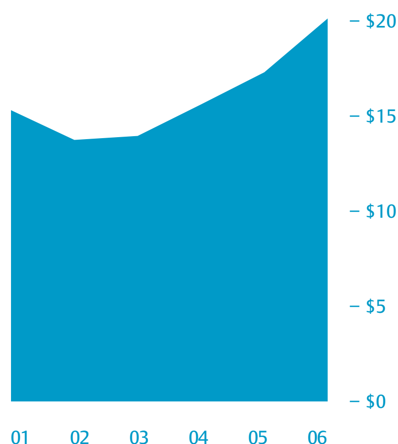
Emerson achieved record sales, earnings and earnings per share in the fiscal year ended September 30, 2006. All of the business segments generated higher sales and earnings compared to the prior year. The Network Power, Process Management and Industrial Automation businesses drove gains in a favorable economic environment as gross fixed investment expanded moderately during 2006. Strong growth in the United States and Asia, solid growth in Europe and acquisitions contributed to these results. Profit margins remained strong primarily due to leverage on higher sales volume and benefits derived from previous cost reduction actions. Emerson's financial position remains strong and the Company continues to generate substantial cash flow.

NET SALES

Net sales for fiscal 2006 were a record $20.1 billion, an increase of approximately $2.8 billion, or 16 percent, over fiscal 2005, with both U.S. and international sales contributing to this growth. The consolidated results reflect increases in all five business segments with an underlying sales (which exclude acquisitions, divestitures and foreign currency translation) increase of more than 12 percent ($2,119 million), an approximate 4 percent ($766 million) contribution from acquisitions and a slightly unfavorable impact ($57 million) from foreign currency translation. The underlying sales increase of more than 12 percent was driven by 12 percent growth in the United States and a total international sales increase of 13 percent. The U.S. market growth was very strong in the first half of 2006 and began to moderate toward the end of the fiscal year, while Europe grew stronger as the year progressed and finished very strong in the fourth quarter. The international sales increase primarily reflects growth in Asia (20 percent) and Europe (7 percent). The Company estimates that the underlying sales growth primarily reflects a nearly 9 percent gain from volume, an approximate 3 percent impact from market penetration gains and a less than 1 percent impact from higher sales prices.

Net sales for fiscal 2005 were $17.3 billion, an increase of approximately $1.7 billion, or 11 percent, over fiscal 2004, with growth in both the U.S. and international markets. Continued strength in commercial and industrial demand and increases in all of the business segments drove the consolidated results, with an underlying sales increase of 6 percent ($895 million), a 2 percent ($257 million) favorable impact from a stronger Euro and other currencies, and an over 3 percent ($552 million) positive impact from acquisitions. The underlying sales increase of 6 percent was driven by 6 percent growth in the United States (including a strong finish to the year with 10 percent growth in the fourth quarter) and a total international sales growth of 6 percent, which primarily reflects 11 percent growth in Asia. The Company estimates that the underlying sales growth primarily reflects an approximate 4 percent gain from volume, an approximate 1 percent impact from market penetration gains and an approximate 1 percent impact from higher sales prices.

SALES *(dollars in billions)*



Emerson achieved record sales of $20.1 billion in 2006. All of the business segments generated higher sales over the prior year.

INTERNATIONAL SALES

International destination sales, including U.S. exports, increased approximately 17 percent, to $9.5 billion in 2006, representing 47 percent of the Company's total sales. U.S. exports were up 13 percent compared to 2005, at $1,127 million. International subsidiary sales, including shipments to the United States, were $8.7 billion in 2006, up 17 percent over 2005. Excluding the net 1 percent unfavorable impact from acquisitions and foreign currency translation, international subsidiary sales increased 18 percent compared to 2005. Underlying destination sales grew 20 percent in Asia during the year, driven mainly by 19 percent growth in China, and 21 percent in Latin America and the Middle East, while sales grew 7 percent in Europe.

International destination sales, including U.S. exports, increased approximately 11 percent, to $8.2 billion in 2005, representing 47 percent of the Company's total sales. U.S. exports were up 6 percent compared to 2004, at $998 million. International subsidiary sales, including shipments to the United States, were $7.4 billion in 2005, up 12 percent over 2004. Excluding the net 4 percent impact from acquisitions and favorable foreign currency translation, international subsidiary sales increased 8 percent compared to 2004. Underlying destination sales grew 11 percent in Asia during the year, driven mainly by 14 percent growth in China, while sales grew 15 percent in Latin America and 10 percent in the Middle East and sales in Europe were flat compared to 2004.

ACQUISITIONS AND DIVESTITURES

The Company acquired Artesyn Technologies, Inc. (Artesyn), Knürr AG (Knürr) and Bristol Babcock (Bristol), as well as several smaller businesses during 2006. Artesyn is a global manufacturer of advanced power conversion equipment and board-level computing solutions for infrastructure applications in telecommunication and data-communication systems. Knürr is a manufacturer of indoor and outdoor enclosure systems and cooling technologies for telecommunications, electronics and computing equipment. Bristol is a manufacturer of control and measurement equipment for oil and gas, water and wastewater, and power industries. Total cash paid for these businesses (net of cash and equivalents acquired of approximately $120 million and debt assumed of approximately $90 million) was approximately $752 million. Annualized sales for acquired businesses were $920 million in 2006.

In 2006, the Company divested or had plans to divest several small business units, including the materials testing business. These businesses had total annual sales of $171 million, $174 million and $204 million for fiscal years 2006, 2005 and 2004, respectively, and earnings were approximately break-even. The Company recorded an after-tax gain of $22 million from the sale of the materials testing business in the fourth quarter of 2006. The sales of the other businesses are expected to close in 2007. These businesses were not reclassified as discontinued operations due to immateriality.

During 2005, the Company acquired Do+Able, a manufacturer of ready-to-assemble storage products, and Numatics, a manufacturer of pneumatic and motion control products, and several smaller businesses. Total cash paid for these businesses (including assumed debt of approximately $100 million, which was repaid in October 2005) was approximately $466 million. During 2004, the Company acquired the North American outside plant and power systems business of Marconi Corporation PLC, as well as several other smaller businesses for a total of approximately $414 million in cash. Annualized sales for acquired businesses were $430 million in both 2005 and 2004. See Note 3 for additional information regarding acquisitions and divestitures.

COST OF SALES

Cost of sales for fiscal 2006 and 2005 were $12.9 billion and $11.1 billion, respectively. Cost of sales as a percent of net sales was 64.4 percent for 2006, compared with 64.3 percent in 2005. Gross profit was $7.2 billion and $6.2 billion for fiscal 2006 and 2005, respectively, resulting in gross profit margins of 35.6 percent and 35.7 percent. The increase in the gross profit primarily reflects higher sales volume and acquisitions. The gross profit margin was unfavorably impacted as leverage on higher sales and benefits realized from productivity improvements were more than offset by higher costs for wages and benefits (pension), negative product mix, as well as the lower profit margin on recent acquisitions. Sales price increases initiated over the past year, together with the benefits received from commodity hedging of approximately $130 million, offset the higher level of raw material costs, but the margin was diluted. Assuming commodity costs remain at these levels, the Company will need to address commodity inflation pressures (particularly copper and steel) with additional procurement initiatives and sales price actions.

Cost of sales for fiscal 2005 and 2004 were $11.1 billion and $10.0 billion, respectively. Cost of sales as a percent of net sales was 64.3 percent for 2005, compared with 64.4 percent in 2004. The gross profit margin increased from 35.6 percent in 2004 to 35.7 percent for 2005 primarily as a result of increased volume and leverage on higher sales, as well as benefits realized from prior rationalization and productivity improvements. Across the Company, higher costs for raw materials were substantially recovered through increases in sales prices, which partially offset these improvements.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

Selling, general and administrative (SG&A) expenses for 2006 were $4.1 billion, or 20.4 percent of net sales, compared with $3.6 billion, or 20.7 percent of net sales for 2005. The increase of approximately $0.5 billion was primarily due to the increase in variable costs on higher sales and acquisitions. The reduction in SG&A as a percent of sales was primarily the result of leveraging fixed costs on higher sales.

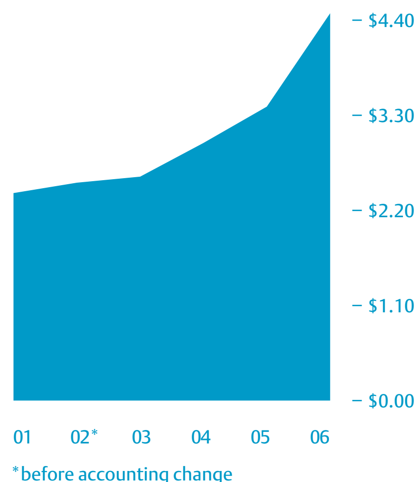
SG&A expenses for 2005 were $3.6 billion compared with $3.3 billion for 2004. As a percent of net sales, SG&A expenses were 20.7 percent in 2005 and 21.0 percent in 2004. Leverage on higher sales and the benefits realized from prior rationalization efforts were partially offset by higher costs for wages and benefits.

OTHER DEDUCTIONS, NET

Other deductions, net were $178 million in 2006, a $52 million decrease from the $230 million in 2005. The decrease primarily reflects $42 million of higher gains in 2006 compared to 2005 and lower rationalization costs. Gains in 2006 included approximately $31 million related to the divesture of the materials testing business and approximately $26 million related to the sale of shares in MKS Instruments, Inc. (MKS). The Company expects to continue liquidating its remaining MKS investment valued at approximately $90 million (cost basis approximately $70 million). Ongoing costs for the rationalization of operations were $84 million in 2006, down from $110 million in 2005, reflecting lower costs, particularly for the Network Power segment. The higher gains and lower rationalization costs were partially offset by higher amortization of intangibles related to acquisitions.

Other deductions, net were $230 million in 2005 compared to $223 million in 2004. In 2005, ongoing costs for the rationalization of operations were $110 million, down from $129 million in 2004, primarily reflecting lower costs in the Process Management and Appliance and Tools segments. The decrease in rationalization costs was more than offset by higher amortization of intangibles, a litigation settlement in 2005 and a 2004 insurance recovery and interest refund. See Notes 4 and 5 for further details regarding other deductions, net and rationalization costs.

EARNINGS PER SHARE



Earnings per share was a record $4.48 in 2006, a 32 percent increase over the prior year.

INTEREST EXPENSE, NET

Interest expense, net was $207 million, $209 million and $210 million in 2006, 2005 and 2004, respectively. During 2006, $250 million of 6.3% notes matured. During 2005, the Company issued $250 million of 4.75% ten-year notes due October 2015, and $600 million of 7 7/8% notes matured.

EARNINGS BEFORE INCOME TAXES

Earnings before income taxes were $2.7 billion for 2006, an increase of 25 percent, compared to $2.1 billion for 2005. The earnings results reflect increases in all five business segments, including $207 million in Process Management, $111 million in Network Power and $105 million in Industrial Automation. The higher earnings also reflect leverage from higher sales, benefits realized from productivity improvements, and higher sales prices, partially offset by higher raw material, wage and benefit costs.

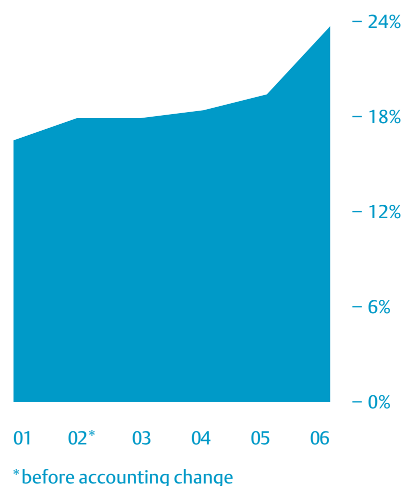
Earnings before income taxes were $2.1 billion for 2005, an increase of 16 percent, compared to $1.9 billion for 2004. The earnings results reflect increases in four of the five business segments, with particular strength in the Network Power, Process Management and Industrial Automation businesses. The higher earnings also reflect increased volume and leverage from the higher sales, savings from cost reduction efforts, and higher sales prices, partially offset by higher raw material costs, higher wage and benefit costs and other items.

INCOME TAXES

Income taxes for 2006 were $839 million compared to $727 million for 2005. The effective tax rate decreased from 34 percent in 2005 to approximately 31 percent in 2006. The change in the tax rate is primarily due to a 3 percentage point decrease resulting from a $63 million tax expense in 2005 related to the one-time opportunity during 2005 to repatriate foreign earnings at a favorable rate under the American Jobs Creation Act of 2004 (the Act).

Income taxes for 2005 were $727 million compared to $595 million for 2004. The effective tax rate increased from 32 percent in 2004 to approximately 34 percent in 2005. The change in the tax rate is primarily due to the tax expense in 2005 related to the Act as discussed above. See Note 13 for further discussion regarding the impact of the Act.

RETURN ON EQUITY



*before accounting change

Emerson achieved a high level of return on average stockholders' equity in 2006, reaching 23.7 percent for this important measure of performance.

NET EARNINGS AND RETURN ON EQUITY

Net earnings and earnings per share for 2006 increased 30 percent and 32 percent, respectively, to a record $1.8 billion and a record $4.48 per share, compared to $1.4 billion and $3.40 per share in 2005. Net earnings as a percent of net sales were 9.2 percent in 2006 compared to 8.2 percent in 2005. Net earnings for 2005 included a tax expense of $63 million, or $0.15 per share, related to the one-time opportunity to repatriate foreign earnings. The 32 percent increase in earnings per share also reflects the purchase of treasury shares. Return on average stockholders' equity was 23.7 percent and 19.4 percent for 2006 and 2005, respectively.

Net earnings and earnings per share for 2005 increased 13 percent and 14 percent, respectively, to $1.4 billion and $3.40 per share, compared to $1.3 billion and $2.98 per share in 2004. Net earnings as a percent of net sales were 8.2 percent in 2005 compared to 8.1 percent in 2004. Net earnings for 2005 include a tax expense of $63 million, or $0.15 per share, related to the one-time opportunity to repatriate foreign earnings. The 14 percent increase in earnings per share also reflects the purchase of treasury shares. Return on average stockholders' equity was 19.4 percent and 18.4 percent for 2005 and 2004, respectively.

Business Segments

PROCESS MANAGEMENT

(DOLLARS IN MILLIONS)	2004	2005	2006	CHANGE '04 - '05	CHANGE '05 - '06
Sales	$3,703	4,200	**4,875**	13%	**16%**
Earnings	$ 476	671	**878**	41%	**31%**
Margin	12.9%	16.0%	**18.0%**		

2006 vs. 2005 - Sales in the Process Management segment were $4.9 billion in 2006, an increase of $675 million, or 16 percent, over 2005, reflecting higher volume and acquisitions. All of the businesses, including measurement, valves and systems, reported higher sales and earnings (defined as earnings before interest and taxes for the business segments discussion) due to worldwide growth in oil and gas and power projects, as well as expansion in China. The increasing demand for energy is driving capacity expansion and upgrades to existing facilities in the energy sector. Underlying sales increased 13 percent, excluding a 3 percent ($147 million) contribution from the Bristol, Tescom and Mobrey acquisitions, driven by the strong market demand and aided by approximately 2 percent from penetration gains and price. The underlying sales increase reflects growth in all major geographic regions, including the United States (15 percent), Asia (15 percent), Latin America (20 percent) and Europe (6 percent), compared with the prior year. Earnings increased 31 percent to $878 million from $671 million in the prior year, primarily reflecting higher sales volume, as well as acquisitions. The margin increase was primarily due to leverage on higher sales. Sales price increases and material cost containment were offset by higher wages.

2005 vs. 2004 - Sales in the Process Management segment were $4.2 billion in 2005, up $497 million, or 13 percent, over 2004, reflecting stronger market demand for capital goods (including process automation products and systems), penetration gains in excess of 1 percent and acquisitions. Nearly all of the businesses reported sales increases, with sales and earnings particularly strong for the valves and measurement businesses due to growth in oil and gas projects, and expansion in China. Underlying sales increased 9 percent, excluding a 2 percent ($84 million) positive contribution from the Metran, Tescom and Mobrey acquisitions and a 2 percent ($79 million) favorable impact from foreign currency translation. The increase in underlying sales reflects 22 percent growth in Asia, 29 percent growth in Canada, 13 percent growth in Latin America and 5 percent growth in the United States, while sales in Europe increased 1 percent compared with 2004. Volume growth, leverage on the higher sales of approximately 2 percentage points and savings from prior cost reduction efforts drove a 41 percent increase in earnings from $476 million in 2004 to $671 million for 2005.

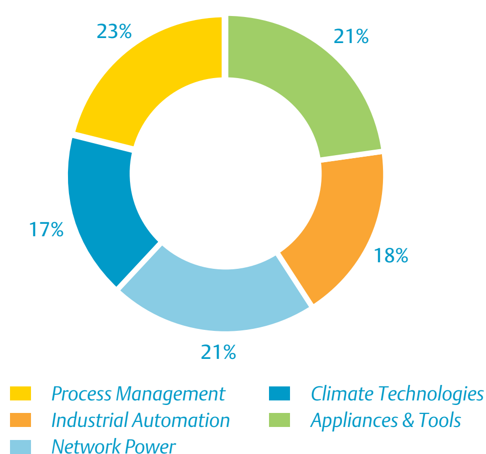
INDUSTRIAL AUTOMATION

(DOLLARS IN MILLIONS)	2004	2005	2006	CHANGE '04 - '05	CHANGE '05 - '06
Sales	$2,936	3,242	**3,767**	10%	**16%**
Earnings	$ 391	464	**569**	19%	**23%**
Margin	13.3%	14.3%	**15.1%**		

2006 vs. 2005 - Sales in the Industrial Automation segment were $3.8 billion in 2006, an increase of 16 percent compared to 2005. Sales grew in all of the major geographic regions and in nearly all of the businesses, reflecting the continued favorable economic environment for capital goods. Underlying sales grew 11 percent, excluding a 6 percent ($208 million) contribution from the Numatics, Saftronics and Jaure acquisitions and a 1 percent ($41 million) unfavorable impact from foreign currency translation. Underlying sales grew 12 percent in the United States and 11 percent internationally. The increase in international sales primarily reflects growth in Europe (10 percent) and Asia (13 percent). The results reflect growth in nearly all of the businesses, with particular strength in the power generating alternator and electrical distribution businesses. The underlying growth reflects both increased global industrial demand and a nearly 3 percent positive impact from price and penetration gains. In addition, the electrical distribution business's strong growth was driven by increased demand in North America, particularly along the Gulf Coast of the United States. Earnings increased 23 percent to $569 million for 2006, compared with $464 million in 2005, reflecting higher sales volume and prices, as well as acquisitions. The margin increase was primarily due to leverage on higher sales volume. Sales price increases and benefits from prior cost reduction efforts were offset by higher material, wage and benefit (pension) costs, as well as dilution from acquisitions. The earnings increase was also aided by an approximate $18 million payment received by the power transmission business from dumping duties related to the U.S. Continued Dumping and Subsidy Offset Act (Offset Act) in the current year, compared with a $13 million payment received in 2005, and lower litigation settlement costs compared to the prior year.

2005 vs. 2004 - Sales in the Industrial Automation segment increased 10 percent compared to 2004 to $3.2 billion in 2005, with sales increases in all of the businesses and major geographic areas, reflecting the favorable economic environment for capital goods. Underlying sales grew nearly 8 percent, excluding a nearly 3 percent ($78 million) favorable impact from foreign currency translation. The underlying sales growth reflects an 11 percent increase in the United States and a 5 percent increase in international sales, with 4 percent growth in Europe, 4 percent growth in Asia and 25 percent growth in the Middle East. The results reflect solid improvements across all the businesses, with particular strength in the power generating alternator and the power transmission businesses, reflecting increased global industrial demand and an estimated 2 percent positive impact from higher sales prices. Earnings increased 19 percent to $464 million for 2005, compared with $391 million in 2004, due to higher sales volume and leverage, while sales price increases nearly offset higher material costs (particularly for steel and copper). The earnings increase was aided by a $13 million payment received by the power transmission business from dumping duties related to the Offset Act in 2005, compared with a $2 million payment received in 2004, partially offset by a litigation settlement related to the electrical products business.

SALES BY SEGMENT



NETWORK POWER

(DOLLARS IN MILLIONS)	2004	2005	**2006**	CHANGE '04 - '05	**CHANGE '05 - '06**
Sales	$2,692	3,317	**4,350**	23%	**31%**
Earnings	$ 297	373	**484**	26%	**30%**
Margin	11.0%	11.2%	**11.1%**		

2006 vs. 2005 - The Network Power segment sales increased 31 percent to $4.4 billion in 2006 compared to $3.3 billion in 2005. End markets were strong across the segment with particular strength in the computing and data-center markets, which led to strong growth in the AC power system and precision cooling businesses. The sales increase reflects 21 percent growth in underlying sales and a 10 percent ($341 million) contribution from the Artesyn and Knürr acquisitions. The underlying sales increase of 21 percent reflects higher volume of approximately 23 percent, of which more than one-third is estimated to be from market penetration gains. These increases were partially offset by an estimated 2 percent impact from lower sales prices. Geographically, underlying sales reflect a 22 percent increase in the United States, a 37 percent increase in Asia (primarily China) and a 3 percent increase in Europe. The Company continues to build upon its Emerson Network Power China division resulting in market penetration in China and other Asian markets. Earnings increased 30 percent, or $111 million, to $484 million, compared with $373 million in 2005, primarily due to higher sales volume. The margin was primarily diluted by the Artesyn acquisition and declines in sales prices, partially offset by material cost containment. Negative product mix in the embedded power business and higher costs related to inventory and warranty in the North American DC power business in the fourth quarter also diluted the margin. Leverage on higher sales volume, savings from prior period cost reduction efforts and a $16 million reduction in rationalization costs versus the prior year mitigated the margin decline.

2005 vs. 2004 - Network Power segment sales increased 23 percent to $3.3 billion in 2005 compared to $2.7 billion in 2004, reflecting acquisitions and continued demand for power systems and precision cooling products, as well as uninterruptible power supplies and original equipment manufacturers (OEM) embedded power modules. Acquisitions added approximately 14 percent ($366 million) to the increase, foreign currency translation had a 1 percent favorable impact, and underlying sales grew 8 percent. The underlying sales increase reflects higher

volume of approximately 7 percent and estimated penetration gains of approximately 4 percent, offset by an estimated 3 percent impact from lower sales prices. Geographically, underlying sales reflect an 11 percent increase in the United States and a 14 percent increase in Asia (primarily China), offset by a 2 percent decrease in Europe. The growth in the United States reflects strong market demand for communications and enterprise computer equipment in 2005. Growth in Asia was driven by increased demand for communications and power equipment, supported by a robust economic environment. Earnings increased 26 percent, or $76 million, to $373 million, compared with $297 million in 2004, primarily reflecting higher sales volume, leverage of approximately 2 percentage points and benefits from prior cost reductions. The earnings increase and margin were impacted by negative price, partially offset by material cost containment. In addition, negative product mix in the embedded power business, as well as integration costs related to the Marconi acquisition, impacted profitability.

CLIMATE TECHNOLOGIES

(DOLLARS IN MILLIONS)	2004	2005	**2006**	CHANGE '04 - '05	**CHANGE '05 - '06**
Sales	$2,983	3,041	**3,424**	2%	**13%**
Earnings	$ 467	453	**523**	(3%)	**15%**
Margin	15.7%	14.9%	**15.3%**		

2006 vs. 2005 - Sales in the Climate Technologies segment were $3.4 billion in 2006, an increase of 13 percent compared to 2005. Underlying sales grew 13 percent, which reflects a 14 percent increase in the United States, a 20 percent increase in Europe and a 1 percent increase in Asia. The underlying sales growth was largely due to strong demand in the air-conditioning compressor business and an estimated 1 percent positive impact from higher sales prices. The volume increase of 12 percent, one-fourth of which is estimated to be from market share gains, was primarily related to scroll compressors. The air-conditioning compressor business was very strong during the year primarily due to demand relating to the transition in the United States to higher efficiency standards that became effective January 23, 2006, as well as weather related demand. Earnings increased 15 percent to $523 million in 2006 compared to $453 million in 2005, primarily due to higher volume. The margin increase reflects leverage on higher sales and savings from prior period cost reduction efforts, partially offset by higher wages and benefits (pension). The margin increase was negatively impacted as the higher sales prices were more than offset by higher material costs. The Company has begun capacity expansion in Mexico where the next generation scroll compressor design and hermetic motors for the North American market will be produced.

2005 vs. 2004 - Climate Technologies segment sales were $3.0 billion in 2005, an increase of 2 percent compared to 2004. Excluding a 1 percent positive impact from foreign currency translation, underlying sales grew 1 percent versus strong 2004 results. Higher sales prices of approximately 2 percent and market share gains were substantially offset by volume decreases due to inventory reductions in the supply chain in the United States and China, as well as decreased wholesaler exports from Europe due to the strong Euro. Sales results for 2005 were mixed across the businesses, with strong growth in U.S. air-conditioning compressors during the fourth quarter driving the overall increase. The growth in the compressor business reflects replenishment of inventories in the distribution channel in the fourth quarter due to late season, warm weather in the United States, as well as anticipatory demand due to the pending transition in the United States to higher efficiency standards. The underlying sales reflect a 3 percent increase in the United States, an 8 percent decline in Europe and a 4 percent decline in Asia, while sales in Latin America increased 35 percent off a smaller base. Earnings from Climate Technologies decreased 3 percent to $453 million in 2005 compared to $467 million in 2004, primarily due to negative impacts from lower sales volume, product mix and higher wage costs, partially offset by benefits from prior cost reduction efforts and lower rationalization costs compared to 2004. Higher sales prices substantially offset higher material costs, which had a dilutive impact on the margin.

APPLIANCE AND TOOLS

(DOLLARS IN MILLIONS)	2004	2005	**2006**	CHANGE '04 - '05	**CHANGE '05 - '06**
Sales	$3,749	4,008	**4,313**	7%	**8%**
Earnings	$ 530	534	**550**	1%	**3%**
Margin	14.1%	13.3%	**12.8%**		

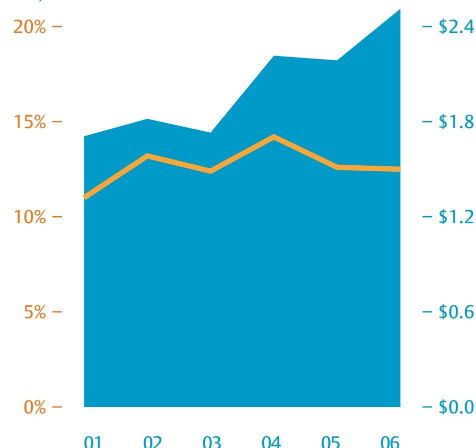
2006 vs. 2005 - The Appliance and Tools segment sales increased 8 percent to $4.3 billion for 2006. This increase reflects 6 percent growth in underlying sales and a 2 percent ($62 million) contribution from the Do+Able acquisition. Sales grew in nearly all of the businesses with most experiencing moderate to strong growth.

Particular strength in the tools, storage and hermetic motors businesses was partially offset by softness in the appliance component business. The hermetic motors business was very strong due to the air-conditioning demand during the year. In addition, the storage businesses showed strong growth driven by the U.S. market. Strength in U.S. residential investment in the first half of 2006 and increased demand at major retailers resulted in continued growth in the storage businesses. The underlying sales increase reflects an estimated 3 percent growth from volume and an approximate 3 percent positive impact from price and penetration gains. Geographically, underlying sales increased 6 percent in the United States and 8 percent internationally. Earnings for 2006 were $550 million, an increase of 3 percent from 2005. The overall increase in profit was partially offset by declines in certain tools, storage and motors businesses, reflecting new product introduction costs in the disposer business, foreign currency losses in the tools and residential storage businesses and restructuring inefficiencies, including costs related to plant shutdown and ramp up of Mexican capacity in the tools and motors businesses. Overall, increases in sales prices were offset by higher raw material (particularly copper, steel and plastics), wage and benefit (pension) costs and negative product mix, diluting the profit margin.

2005 vs. 2004 - Appliance and Tools segment sales increased 7 percent to $4.0 billion for 2005. This increase reflects a 3 percent growth in underlying sales, a 1 percent favorable impact from foreign currency translation and a 3 percent ($101 million) positive impact from Do+Able and a smaller acquisition. Geographically, underlying sales increased 3 percent in the United States and 3 percent internationally. The underlying sales increase primarily reflects an approximate 3 percent positive impact from higher sales prices. The results were mixed across the segment with gains in most of the businesses, particularly strong growth in storage and hermetic motors, and softness in the appliance motor and component businesses. Strong growth in the storage businesses primarily resulted from strength in new and existing home markets as reflected in U.S. residential investment in 2005, and increased demand at major retailers. Earnings of the Appliance and Tools segment for 2005 of $534 million were up 1 percent from 2004, primarily due to $23 million in lower rationalization costs compared to 2004, partially offset by a $12 million negative impact from a quality issue with an appliance component in 2005. Higher sales prices were more than offset by higher raw material costs (particularly steel and copper in the motors business), which together with acquisitions diluted the margin.

OPERATING CASH FLOW AND AS A PERCENT OF SALES

(dollars in billions)



Operating cash flow of $2.5 billion in 2006 enabled Emerson to pay record dividends and buy back 10.7 million shares of common stock.

Financial Position, Capital Resources and Liquidity

The Company continues to generate substantial cash from operations and is in a strong financial position with total assets of $19 billion and stockholders' equity of $8 billion, and has the resources available for reinvestment in existing businesses, strategic acquisitions and managing the capital structure on a short- and long-term basis.

CASH FLOW

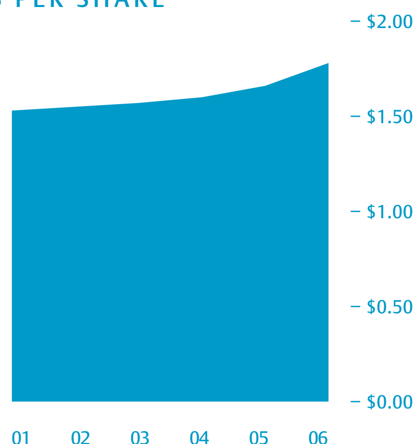
(DOLLARS IN MILLIONS)	2004	2005	2006
Operating Cash Flow	$2,216	2,187	**2,512**
Percent of sales	*14.2%*	*12.6%*	***12.5%***
Capital Expenditures	$ 400	518	**601**
Percent of sales	*2.6%*	*3.0%*	***3.0%***
Free Cash Flow (Operating Cash Flow Less Capital Expenditures)	$1,816	1,669	**1,911**
Percent of sales	*11.6%*	*9.6%*	***9.5%***
Operating Working Capital	$1,633	1,643	**2,044**
Percent of sales	*10.5%*	*9.5%*	***10.1%***

Emerson generated operating cash flow of $2.5 billion in 2006, a 15 percent increase from 2005. Higher net earnings were partially offset by additional working capital necessary to support the higher level of sales. Cash flow in 2006 reflects continued improvements in operating working capital management, including a 2 percent increase in days payable outstanding.

Operating cash flow was $2.2 billion in 2005, a 1 percent decrease from 2004. Higher net earnings were more than offset by additional working capital necessary to support the higher level of sales and the $140 million tax refund in 2004 related to the sale of Jordan stock including its Dura-Line operations in 2003. At September 30, 2006, operating working capital as a percent of sales was 10.1 percent, compared with 9.5 percent and 10.5 percent in 2005 and 2004, respectively. Operating cash flow was decreased by pension contributions of $124 million, $124 million and $167 million in 2006, 2005 and 2004, respectively. Pension contributions are expected to be approximately $100 million to $150 million in 2007.

Free cash flow (operating cash flow less capital expenditures) was $1.9 billion in 2006, compared to $1.7 billion and $1.8 billion in 2005 and 2004, respectively. The 15 percent increase in free cash flow in 2006 compared to 2005 reflects the increase in operating cash flow, primarily due to higher net earnings, partially offset by higher capital spending. The 8 percent decrease in 2005 compared to 2004 was primarily due to higher capital expenditures. Capital expenditures were $601 million, $518 million and $400 million in 2006, 2005 and 2004, respectively. The increase in capital expenditures during 2006 compared to the prior year includes capacity expansion and acquisitions in the Network Power segment, while the increase in 2005 compared to 2004 was primarily driven by unitary air-conditioning scroll compressor capacity expansion in the United States and Asia. In 2007, the Company is targeting capital spending of approximately 3 percent of net sales. Cash paid in connection with Emerson's acquisitions was $752 million, $366 million and $414 million in 2006, 2005 and 2004, respectively.

DIVIDENDS PER SHARE



Dividends increased to a record $1.78 per share in 2006, representing the 50th consecutive year of increased dividends.

Dividends were $730 million ($1.78 per share, up 7 percent) in 2006, compared with $694 million ($1.66 per share) in 2005, and $675 million ($1.60 per share) in 2004. In November 2006, the Board of Directors voted to increase the quarterly cash dividend 18 percent to an annualized rate of $2.10 per share. Also in November 2006, the Company's Board of Directors declared a two-for-one split of the Company's common stock effected in the form of a 100 percent stock dividend to shareholders of record as of November 17, 2006, with a distribution date of December 11, 2006 (shares begin trading on a post-split basis on December 12, 2006). In 2006, approximately 10,726,000 shares were repurchased under the 2002 Board of Directors' authorization; in 2005, approximately 10,035,000 shares were repurchased under the 2002 authorization, and in 2004, approximately 2,630,000 shares were repurchased under the fiscal 1997 and 2002 Board of Directors' authorizations; 16.8 million shares remain available for repurchase under the 2002 authorization and none remain under the 1997 authorization. Purchases of treasury stock totaled $871 million, $671 million and $157 million in 2006, 2005 and 2004, respectively.

LEVERAGE/CAPITALIZATION

(DOLLARS IN MILLIONS)	2004	2005	2006
Total Assets	$16,361	17,227	**18,672**
Long-term Debt	$ 3,136	3,128	**3,128**
Stockholders' Equity	$ 7,238	7,400	**8,154**
Total Debt-to-Capital Ratio	35.8%	35.6%	**33.1%**
Net Debt-to-Net Capital Ratio	27.0%	27.7%	**28.1%**
Operating Cash Flow-to-Debt Ratio	54.9%	53.4%	**62.4%**
Interest Coverage Ratio	8.9	9.8	**12.9**

Total debt was $4.0 billion, $4.1 billion and $4.0 billion for 2006, 2005 and 2004, respectively. The total debt-to-capital ratio was 33.1 percent at year-end 2006, compared with 35.6 percent for 2005 and 35.8 percent for 2004. At September 30, 2006, net debt (total debt less cash and equivalents and short-term investments) was 28.1 percent of net capital, compared with 27.7 percent of net capital in 2005 and 27.0 percent of net capital in 2004. The operating cash flow-to-debt ratio was 62.4 percent, 53.4 percent and 54.9 percent in 2006, 2005 and 2004, respectively. The Company's interest coverage ratio (earnings before income taxes and interest expense, divided by interest expense) was 12.9 times in 2006, compared with 9.8 times in 2005 and 8.9 times in 2004. The increase in the interest coverage ratio over the last three years reflects higher

earnings and lower average borrowings. See Notes 3, 8 and 9 for additional information. The Company's strong financial position supports long-term debt ratings of A2 by Moody's Investors Service and A by Standard and Poor's.

At year-end 2006, the Company maintained a five-year revolving credit facility effective until April 2011 amounting to $2.8 billion to support short-term borrowings. The credit facility does not contain any financial covenants, and is not subject to termination based upon a change in credit ratings or a material adverse change. In addition, as of September 30, 2006, the Company could issue up to $2.25 billion in debt securities, preferred stock, common stock, warrants, share purchase contracts and share purchase units under the shelf registration statement filed with the Securities and Exchange Commission.

CONTRACTUAL OBLIGATIONS

At September 30, 2006, the Company's contractual obligations, including estimated payments due by period, are as follows:

		PAYMENTS DUE BY PERIOD			
(DOLLARS IN MILLIONS)	TOTAL	LESS THAN 1 YEAR	1-3 YEARS	3-5 YEARS	MORE THAN 5 YEARS
Long-term Debt	$3,130	2	726	637	1,765
Operating Leases	509	143	174	89	103
Purchase Obligations	815	676	128	11	–
Total	$4,454	821	1,028	737	1,868

Purchase obligations consist primarily of inventory purchases made in the normal course of business to meet operational requirements. The above table does not include $2.0 billion of other noncurrent liabilities recorded in the balance sheet, as summarized in Note 17, which consist primarily of deferred income tax and retirement and postretirement plan liabilities, because it is not certain when these liabilities will become due. See Notes 10, 11 and 13 for additional information.

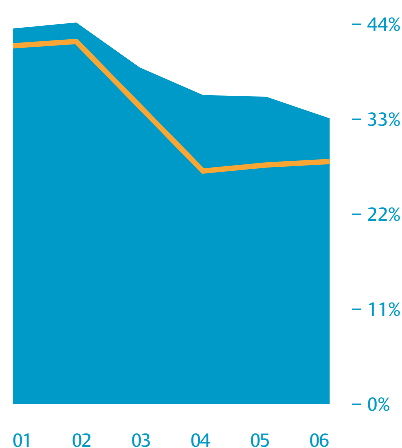
FINANCIAL INSTRUMENTS

The Company is exposed to market risk related to changes in interest rates, copper and other commodity prices and European and other foreign currency exchange rates, and selectively uses derivative financial instruments, including forwards, swaps and purchased options, to manage these risks. The Company does not hold derivatives for trading purposes. The value of market risk sensitive derivative and other financial instruments is subject to change as a result of movements in market rates and prices. Sensitivity analysis is one technique used to evaluate these impacts. Based on a hypothetical ten-percent increase in interest rates, ten-percent decrease in commodity prices or ten-percent weakening in the U.S. dollar across all currencies, the potential losses in future earnings, fair value and cash flows are immaterial. This method has limitations; for example, a weaker U.S. dollar would benefit future earnings through favorable translation of non-U.S. operating results and lower commodity prices would benefit future earnings through lower cost of sales. See Notes 1, 7, 8 and 9.

Critical Accounting Policies

Preparation of the Company's financial statements requires management to make judgments, assumptions and estimates regarding uncertainties that affect the reported amounts of assets, liabilities, stockholders' equity, revenues and expenses. Note 1 of the Notes to Consolidated Financial Statements describes the significant accounting policies used in preparation of the Consolidated Financial Statements. The most significant areas involving management judgments and estimates are described in the following paragraphs. Actual results in these areas could differ materially from management's estimates under different assumptions or conditions.

DEBT AS A PERCENT OF CAPITAL



Total debt was 33 percent of total capital and net debt was 28 percent of net capital at year-end 2006. Emerson maintains a conservative financial structure to provide the strength and flexibility necessary to achieve our strategic objectives.

REVENUE RECOGNITION

The Company recognizes nearly all of its revenues through the sale of manufactured products and records the sale when products are shipped and title passes to the customer and collection is reasonably assured. In certain instances, revenue is recognized on the percentage-of-completion method, when services are rendered, or in accordance with AICPA Statement of Position No. 97-2, "Software Revenue Recognition." Sales sometimes include multiple items including services such as installation. In such instances, revenue assigned to each item is based on that item's objectively determined fair value, and revenue is recognized individually for delivered items only if the delivered items have value to the customer on a standalone basis, performance of the undelivered items is probable and substantially in the Company's control and the undelivered items are inconsequential or perfunctory. Management believes that all relevant criteria and conditions are considered when recognizing sales.

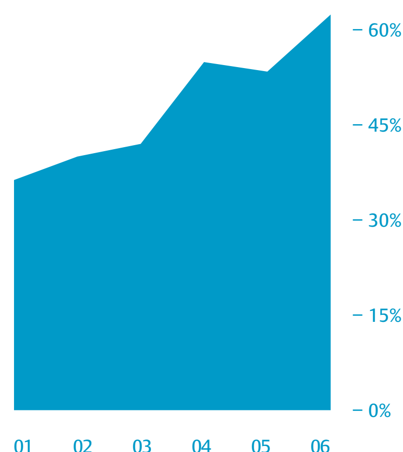
INVENTORIES

Inventories are stated at the lower of cost or market. The majority of inventory values are based upon standard costs which approximate average costs, while the remainder are principally valued on a first-in, first-out basis. Standard costs are revised at the beginning of each fiscal year. The effects of resetting standards and operating variances incurred during each period are allocated between inventories and cost of sales. Management regularly reviews inventory for obsolescence to determine whether a write-down is necessary. Various factors are considered in making this determination, including recent sales history and predicted trends, industry market conditions and general economic conditions. See Note 1.

LONG-LIVED ASSETS

Long-lived assets, which include primarily goodwill and property, plant and equipment, are reviewed for impairment whenever events or changes in business circumstances indicate the carrying value of the assets may not be recoverable. If the Company determines that the carrying value of the long-lived asset may not be recoverable, a permanent impairment charge is recorded for the amount by which the carrying value of the long-lived asset exceeds its fair value. Fair value is generally measured based on a discounted cash flow method using a discount rate determined by management to be commensurate with the risk inherent in the Company's current business model. The estimates of cash flows and discount rate are subject to change due to the economic environment, including such factors as interest rates, expected market returns and volatility of markets served. Management believes that the estimates of future cash flows and fair value are reasonable; however, changes in estimates could materially affect the evaluations. See Notes 1, 3 and 6.

OPERATING CASH FLOW TO TOTAL DEBT



Strong cash flow performance in 2006 increased the ratio of operating cash flow to total debt to 62 percent.

RETIREMENT PLANS

Defined benefit plan expense and obligations are dependent on assumptions used in calculating such amounts. These assumptions include discount rate, rate of compensation increases and expected return on plan assets. In accordance with U.S. generally accepted accounting principles, actual results that differ from the assumptions are accumulated and amortized over future periods. While management believes that the assumptions used are appropriate, differences in actual experience or changes in assumptions may affect the Company's retirement plan obligations and future expense. Effective for 2007, the discount rate for the U.S. retirement plans was adjusted to 6.5 percent based on the changes in market interest rates. Defined benefit pension plan expense is expected to decrease approximately $20 million in 2007. The Company is analyzing the impact of adopting Statement of Financial Accounting Standards No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans – an amendment of FASB Statements No. 87, 88, 106 and 132(R)" (FAS 158), and estimates that if the provisions of FAS 158 were applied as of September 30, 2006, an after-tax charge to equity of approximately $500 million ($800 million pretax) would have been reported. See further discussion of FAS

158 under the New Accounting Pronouncements section below. The Company contributed $124 million to defined benefit plans in 2006 and expects to contribute approximately $100 million to $150 million in 2007. See Note 10.

INCOME TAXES

Income tax expense and deferred tax assets and liabilities reflect management's assessment of actual future taxes to be paid on items reflected in the financial statements. Deferred tax assets and liabilities are measured using enacted tax rates in effect for the year in which the temporary differences between the consolidated financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the period that includes the enactment date. No provision is made for U.S. income taxes on the undistributed earnings of non-U.S. subsidiaries. These earnings are permanently invested or otherwise indefinitely retained for continuing international operations. Determination of the amount of taxes that might be paid on these undistributed earnings if eventually remitted is not practicable. See Note 13.

The American Jobs Creation Act of 2004 (the Act) was signed into law on October 22, 2004. The Act repeals an export tax benefit, provides for a 9 percent deduction on U.S. manufacturing income, and allows the repatriation of foreign earnings at a reduced rate for one year, subject to certain limitations. When fully phased-in, management estimates that the repeal of the export tax benefit will be offset by the deduction on manufacturing income. During 2005, the Company repatriated approximately $1.4 billion ($1.8 billion in total) of cash from undistributed earnings of non-U.S. subsidiaries under the Act. As a result, the Company recorded a tax expense of $63 million, or $0.15 per share, in 2005.

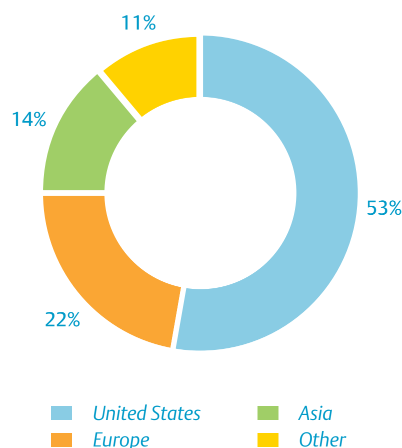
NEW ACCOUNTING PRONOUNCEMENTS

In June 2006, the Financial Accounting Standards Board issued Interpretation No. 48, "Accounting for Uncertainty in Income Taxes – an Interpretation of FASB Statement 109" (FIN 48). FIN 48 addresses the accounting for uncertain tax positions that a company has taken or expects to take on a tax return. The Company is in the process of analyzing the impact of FIN 48, which is required to be adopted by the first quarter of fiscal 2008. FIN 48 is not expected to have a material impact on the financial statements.

In September 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 157, "Fair Value Measurements" (FAS 157). FAS 157 defines fair value, establishes a formal framework for measuring fair value and expands disclosures about fair value measurements. The Company is in the process of analyzing the impact of FAS 157, which is effective for fiscal years beginning after November 15, 2007.

In September 2006, the Financial Accounting Standards Board issued FAS 158. FAS 158 requires employers to recognize the over- or under-funded status of defined benefit plans and other postretirement plans in the statement of financial position and to recognize changes in the funded status in the year in which the changes occur through comprehensive income. In addition, FAS 158 requires employers to measure the funded status of plans as of the date of the year-end statement of financial position. The recognition and disclosure provisions of FAS 158 are effective for fiscal years ending after December 15, 2006, while the requirement to measure plan assets and benefit obligations as of a company's year-end date is effective for fiscal years ending after December 15, 2008. The Company is currently in the process of analyzing the impact of FAS 158; however, see the previous discussion under Critical Accounting Policies for the potential impact on the Company's financial statements upon adoption.

SALES BY GEOGRAPHIC DESTINATION



Consolidated Statements of Earnings

EMERSON ELECTRIC CO. & SUBSIDIARIES

Years ended September 30 | Dollars in millions, except per share amounts

	2004	2005	2006
Net sales	$15,615	17,305	**20,133**
Costs and expenses:			
Cost of sales	10,049	11,122	**12,965**
Selling, general and administrative expenses	3,281	3,595	**4,099**
Other deductions, net	223	230	**178**
Interest expense (net of interest income: 2004, $24; 2005, $34; 2006, $18)	210	209	**207**
Earnings before income taxes	1,852	2,149	**2,684**
Income taxes (2005 includes a $63 expense for repatriation under the American Jobs Creation Act)	595	727	**839**
Net earnings	$ 1,257	1,422	**1,845**
Basic earnings per common share	$ 3.00	3.43	**4.52**
Diluted earnings per common share	$ 2.98	3.40	**4.48**

See accompanying Notes to Consolidated Financial Statements.

Consolidated Balance Sheets

EMERSON ELECTRIC CO. & SUBSIDIARIES

September 30 | Dollars in millions, except per share amounts

ASSETS	2005	**2006**
Current assets		
Cash and equivalents	$ 1,233	**810**
Receivables, less allowances of $76 in 2005 and $74 in 2006	3,256	**3,716**
Inventories:		
Finished products	711	**887**
Raw materials and work in process	1,102	**1,335**
Total inventories	1,813	**2,222**
Other current assets	535	**582**
Total current assets	6,837	**7,330**
Property, plant and equipment		
Land	185	**188**
Buildings	1,426	**1,536**
Machinery and equipment	5,442	**5,811**
Construction in progress	303	**354**
	7,356	**7,889**
Less accumulated depreciation	4,353	**4,669**
Property, plant and equipment, net	3,003	**3,220**
Other assets		
Goodwill	5,479	**6,013**
Other	1,908	**2,109**
Total other assets	7,387	**8,122**
	$17,227	**18,672**

See accompanying Notes to Consolidated Financial Statements.

LIABILITIES AND STOCKHOLDERS' EQUITY	2005	2006
Current liabilities		
Short-term borrowings and current maturities of long-term debt	$ 970	**898**
Accounts payable	1,841	**2,305**
Accrued expenses	1,839	**1,933**
Income taxes	281	**238**
Total current liabilities	4,931	**5,374**
Long-term debt	3,128	**3,128**
Other liabilities	1,768	**2,016**
Stockholders' equity		
Preferred stock of $2.50 par value per share		
Authorized 5,400,000 shares; issued – none	—	**—**
Common stock of $0.50 par value per share		
Authorized 1,200,000,000 shares; issued 476,677,006 shares;		
outstanding 410,651,564 shares in 2005 and 402,346,899 shares in 2006	238	**238**
Additional paid-in capital	120	**161**
Retained earnings	10,199	**11,314**
Accumulated other comprehensive income	(65)	**306**
	10,492	**12,019**
Less cost of common stock in treasury, 66,025,442 shares in 2005 and		
74,330,107 shares in 2006	3,092	**3,865**
Total stockholders' equity	7,400	**8,154**
	$17,227	**18,672**

Consolidated Statements of Stockholders' Equity

EMERSON ELECTRIC CO. & SUBSIDIARIES

Years ended September 30 | Dollars in millions, except per share amounts

	2004	2005	**2006**
Common stock	$ 238	238	**238**
Additional paid-in capital			
Beginning balance	65	87	**120**
Stock plans and other	22	33	**41**
Ending balance	87	120	**161**
Retained earnings			
Beginning balance	8,889	9,471	**10,199**
Net earnings	1,257	1,422	**1,845**
Cash dividends (per share: 2004, $1.60; 2005, $1.66; 2006, $1.78)	(675)	(694)	**(730)**
Ending balance	9,471	10,199	**11,314**
Accumulated other comprehensive income			
Beginning balance	(386)	(88)	**(65)**
Foreign currency translation	264	11	**175**
Minimum pension liability (net of tax of: 2004, $(24); 2005, $10; 2006, $(71))	32	(18)	**121**
Cash flow hedges and other (net of tax of: 2004, $(2); 2005, $(17); 2006, $(43))	2	30	**75**
Ending balance	(88)	(65)	**306**
Treasury stock			
Beginning balance	(2,346)	(2,470)	**(3,092)**
Acquired	(157)	(671)	**(871)**
Issued under stock plans and other	33	49	**98**
Ending balance	(2,470)	(3,092)	**(3,865)**
Total stockholders' equity	$ 7,238	7,400	**8,154**
Comprehensive income (Net earnings and changes in Foreign currency translation, Minimum pension liability and Cash flow hedges)	$ 1,555	1,445	**2,216**

See accompanying Notes to Consolidated Financial Statements.

Consolidated Statements of Cash Flows

EMERSON ELECTRIC CO. & SUBSIDIARIES

Years ended September 30 | Dollars in millions

	2004	2005	2006
Operating Activities			
Net earnings	$1,257	1,422	**1,845**
Adjustments to reconcile net earnings to net cash provided by operating activities:			
Depreciation and amortization	557	562	**607**
Changes in operating working capital	322	110	**(152)**
Pension funding	(167)	(124)	**(124)**
Other	247	217	**336**
Net cash provided by operating activities	2,216	2,187	**2,512**
Investing activities			
Capital expenditures	(400)	(518)	**(601)**
Purchases of businesses, net of cash and equivalents acquired	(414)	(366)	**(752)**
Other	126	(12)	**137**
Net cash used in investing activities	(688)	(896)	**(1,216)**
Financing activities			
Net increase (decrease) in short-term borrowings	(106)	320	**89**
Proceeds from long-term debt	29	251	**6**
Principal payments on long-term debt	(16)	(625)	**(266)**
Dividends paid	(675)	(694)	**(730)**
Purchases of treasury stock	(149)	(668)	**(862)**
Other	(1)	15	**32**
Net cash used in financing activities	(918)	(1,401)	**(1,731)**
Effect of exchange rate changes on cash and equivalents	40	(3)	**12**
Increase (decrease) in cash and equivalents	650	(113)	**(423)**
Beginning cash and equivalents	696	1,346	**1,233**
Ending cash and equivalents	$1,346	1,233	**810**
Changes in operating working capital			
Receivables	$ (134)	(261)	**(246)**
Inventories	(8)	8	**(274)**
Other current assets	202	(44)	**36**
Accounts payable	123	161	**324**
Accrued expenses	114	77	**71**
Income taxes	25	169	**(63)**
	$ 322	110	**(152)**

See accompanying Notes to Consolidated Financial Statements.

Notes to Consolidated Financial Statements

EMERSON ELECTRIC CO. & SUBSIDIARIES

Years ended September 30 | Dollars in millions, except per share amounts

(1) Summary of Significant Accounting Policies

PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of the Company and its controlled affiliates. All significant intercompany transactions, profits and balances are eliminated in consolidation. Other investments of 20 percent to 50 percent are accounted for by the equity method. Investments in nonpublicly-traded companies of less than 20 percent are carried at cost. Investments in publicly-traded companies of less than 20 percent are carried at fair value, with changes in fair value reflected in accumulated other comprehensive income.

FOREIGN CURRENCY TRANSLATION

The functional currency of a vast majority of the Company's non-U.S. subsidiaries is the local currency. Adjustments resulting from the translation of financial statements are reflected in accumulated other comprehensive income.

CASH EQUIVALENTS

Cash equivalents consist of highly liquid investments with original maturities of three months or less.

INVENTORIES

Inventories are stated at the lower of cost or market. The majority of inventory values are based upon standard costs which approximate average costs, while the remainder are principally valued on a first-in, first-out basis. Standard costs are revised at the beginning of each fiscal year. The effects of resetting standards and operating variances incurred during each period are allocated between inventories and cost of sales.

PROPERTY, PLANT AND EQUIPMENT

The Company records investments in land, buildings, and machinery and equipment at cost. Depreciation is computed principally using the straight-line method over estimated service lives. Service lives for principal assets are 30 to 40 years for buildings and 8 to 12 years for machinery and equipment. Long-lived assets are reviewed for impairment whenever events or changes in business circumstances indicate the carrying value of the assets may not be recoverable. Impairment losses are recognized based on fair value if expected future cash flows of the related assets are less than their carrying values.

GOODWILL AND INTANGIBLE ASSETS

Assets and liabilities acquired in business combinations are accounted for using the purchase method and recorded at their respective fair values. Substantially all goodwill is assigned to the reporting unit that acquires a business. A reporting unit is an operating segment as defined in Statement of Financial Accounting Standards No. 131, "Disclosures about Segments of an Enterprise and Related Information," or a business one level below an operating segment if discrete financial information is prepared and regularly reviewed by the segment manager. The Company conducts a formal impairment test of goodwill on an annual basis and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying value. Under the impairment test, if a reporting unit's carrying amount exceeds its estimated fair value, a goodwill impairment is recognized to the extent that the reporting unit's carrying amount of goodwill exceeds the implied fair value of the goodwill. Fair values of reporting units are estimated using discounted cash flows and market multiples.

All of the Company's intangible assets (other than goodwill) are subject to amortization. Intangibles consist of intellectual property (such as patents and trademarks), customer relationships and capitalized software and are amortized on a straight-line basis. These intangibles are also subject to evaluation for potential impairment if an event occurs or circumstances change that indicate the carrying amount may not be recoverable.

WARRANTY

The Company's product warranties vary by each of its product lines and are competitive for the markets in which it operates. Warranty generally extends for a period of one to two years from the date of sale or installation. Provisions for warranty are determined primarily based on historical warranty cost as a percentage of sales or a fixed amount per unit sold based on failure rates, adjusted for specific problems that may arise. Product warranty expense is less than 1 percent of sales.

REVENUE RECOGNITION

The Company recognizes nearly all of its revenues through the sale of manufactured products and records the sale when products are shipped and title passes to the customer and collection is reasonably assured. In certain instances, revenue is recognized on the percentage-of-completion method, when services are rendered, or in accordance with AICPA Statement of Position No. 97-2, "Software Revenue Recognition." Sales sometimes include multiple items including services such as installation. In such instances, revenue assigned to each item is based on that item's objectively determined fair value, and revenue is recognized individually for delivered items only if the delivered items have value to the customer on a standalone basis, performance of the undelivered items is probable and substantially in the Company's control and the undelivered items are inconsequential or perfunctory. Management believes that all relevant criteria and conditions are considered when recognizing sales.

STOCK-BASED COMPENSATION

Effective October 1, 2002, Emerson adopted the fair value method provisions of Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation." Under the Standard's prospective method of adoption, options granted, modified, or settled after September 30, 2002, are expensed based on their fair value at date of grant over the vesting period, generally three years. Previously, the Company accounted for options pursuant to Accounting Principles Board Opinion No. 25, and no expense was recognized. Effective July 1, 2005, Emerson adopted Statement of Financial Accounting Standards No. 123 (revised 2004), "Share-Based Payment" (FAS 123R), under the Standard's modified prospective method, and FAS 123R did not have a material impact on the financial statements. The following table illustrates the effect on 2005 and 2004 net earnings and earnings per share if the fair value based method had been applied to all outstanding and unvested awards. The adoption of FAS 123R did not have an impact in 2006.

	2004	2005
Net earnings, as reported	$1,257	1,422
Add: Stock-based employee compensation expense included in reported net earnings, net of related tax effects	42	65
Deduct: Total stock-based employee compensation expense determined under the fair value based method for all awards, net of related tax effects	48	67
Pro forma net earnings	$1,251	1,420
Earnings per share:		
Basic – as reported	$ 3.00	3.43
Basic – pro forma	$ 2.99	3.42
Diluted – as reported	$ 2.98	3.40
Diluted – pro forma	$ 2.97	3.39

See Note 14 for more information regarding stock-based compensation.

FINANCIAL INSTRUMENTS

All derivative instruments are reported on the balance sheet at fair value. For each derivative instrument designated as a cash flow hedge, the gain or loss on the derivative is deferred in accumulated other comprehensive income until recognized in earnings with the underlying hedged item. For each derivative instrument designated as a fair value hedge, the gain or loss on the derivative and the offsetting gain or loss on the hedged item are recognized immediately in earnings. Currency fluctuations on non-U.S. dollar obligations that have been designated as hedges on non-U.S. net asset exposures are included in accumulated other comprehensive income.

INCOME TAXES

No provision is made for U.S. income taxes on the undistributed earnings of non-U.S. subsidiaries (approximately $2.5 billion at September 30, 2006). These earnings are permanently invested or otherwise indefinitely retained for continuing international operations. Determination of the amount of taxes that might be paid on these undistributed earnings if eventually remitted is not practicable. During 2005, the Company repatriated approximately $1.4 billion ($1.8 billion in total) of cash from undistributed earnings of non-U.S. subsidiaries under the American Jobs Creation Act of 2004 and recorded a tax expense of $63.

COMPREHENSIVE INCOME

Comprehensive income is primarily comprised of net earnings and changes in foreign currency translation, minimum pension liability and cash flow hedges. Accumulated other comprehensive income, after-tax, consists of foreign currency translation credits of $269 and $94, minimum pension liability charges of $57 and $178, and cash flow hedges and other credits of $94 and $19 at September 30, 2006 and 2005, respectively.

FINANCIAL STATEMENT PRESENTATION

The preparation of the financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect reported amounts and related disclosures. Actual results could differ from those estimates. Certain prior year amounts have been reclassified to conform to the current year presentation.

(2) Weighted Average Common Shares

Basic earnings per common share consider only the weighted average of common shares outstanding while diluted earnings per common share consider the dilutive effects of stock options, incentive shares and convertible securities. Options to purchase approximately 0.5 million, 2.6 million and 1.0 million shares of common stock were excluded from the computation of diluted earnings per share in 2006, 2005 and 2004, respectively, because their effect would have been antidilutive. Reconciliations of weighted average common shares for basic earnings per common share and diluted earnings per common share follow:

(SHARES IN MILLIONS)	2004	2005	**2006**
Basic	419.3	414.9	**408.3**
Dilutive shares	2.9	4.0	**3.9**
Diluted	422.2	418.9	**412.2**

(3) Acquisitions and Divestitures

The Company acquired Artesyn Technologies, Inc. (Artesyn) during the third quarter of fiscal 2006, and Knürr AG (Knürr) and Bristol Babcock (Bristol) during the second quarter of fiscal 2006. Artesyn is a global manufacturer of advanced power conversion equipment and board-level computing solutions for infrastructure applications in telecommunication and data-communication systems and is included in the Network Power segment. Knürr is a manufacturer of indoor and outdoor enclosure systems and cooling technologies for telecommunications, electronics and computing equipment and is included in the Network Power segment. Bristol is a manufacturer of control and measurement equipment for oil and gas, water and wastewater, and power industries and is included in the Process Management segment. In addition to Artesyn, Knürr and Bristol, the Company acquired several smaller businesses during 2006 mainly in the Industrial Automation and Appliance and Tools segments. Total cash paid for these businesses (net of cash and equivalents acquired of approximately $120 and debt assumed of approximately $90) and annualized sales were approximately $752 and $920, respectively. Goodwill of $481 ($54 of which is expected to be deductible for tax purposes) and identifiable intangible assets (primarily technology and customer relationships) of $189, which are being amortized on a straight-line basis over a weighted-average life of nine years, were recognized from these transactions in 2006. Third-party valuations of assets are in-process; purchase price allocations are subject to refinement.

In 2006, the Company divested or had plans to divest several business units, including the materials testing business. These businesses had total annual sales of $171, $174 and $204 for fiscal years 2006, 2005 and 2004, respectively, and earnings were approximately break-even. The Company recorded a pretax gain of $31 ($22 after-tax) from the sale of the materials testing business in the fourth quarter of 2006. The sales of the other business units are expected to close in 2007, and the units were written down to their net realizable values, which resulted in a charge of $14 ($2 after-tax) in the fourth quarter of 2006. These businesses were not reclassified as discontinued operations due to immateriality.

The Company acquired Do+Able, a manufacturer of ready-to-assemble wood and steel home and garage organization and storage products, which is included in the Appliance and Tools segment, in the second quarter of 2005 and Numatics, a manufacturer of pneumatic and motion control products for industrial applications, which is included in the Industrial Automation segment, in the fourth quarter of 2005. In addition to Do+Able and Numatics, the Company acquired several smaller businesses during 2005, mainly in the Process Management and Appliance and Tools segments. Total cash paid (including assumed debt of approximately $100, which was

repaid in October 2005) and annualized sales for these businesses were approximately $466 and $430, respectively. Goodwill of $236 ($58 of which is expected to be deductible for tax purposes) and identifiable intangible assets of $122, which are being amortized on a straight-line basis over a weighted-average useful life of ten years, were recognized from these transactions in 2005.

In the fourth quarter of 2004, the Company acquired the outside plant and power systems business of Marconi Corporation PLC, a leading provider of DC power products and engineering and installation services to major telecommunication carriers throughout North America, which is included in the Network Power segment. Marconi (renamed Emerson Network Power Energy Systems – North America) and several smaller businesses acquired during 2004 for a total of $414 in cash (net of cash and equivalents acquired) had annualized sales of approximately $430. Goodwill of $224 (substantially all of which is expected to be deductible for tax purposes) and identifiable intangible assets of $120 (all of which is being amortized on a straight-line basis with a weighted-average life of 14 years) were recognized from these transactions.

The results of operations of these businesses have been included in the Company's consolidated results of operations since the respective dates of acquisition and prior to the respective dates of divestiture.

(4) Other Deductions, Net

Other deductions, net are summarized as follows:

	2004	2005	**2006**
Rationalization of operations	$129	110	**84**
Amortization of intangibles (intellectual property and customer relationships)	21	28	**47**
Other	100	118	**115**
Gains, net	(27)	(26)	**(68)**
Total	$223	230	**178**

Other is comprised of several items which are individually immaterial, including minority interest expense, foreign currency gains and losses, bad debt expense, equity investment income and losses, as well as one-time items, such as litigation and disputed matters, insurance recoveries and interest refunds.

Gains, net for 2006 includes the following items. The Company recorded gains of approximately $26 in 2006 related to the sale of 4.4 million shares of MKS Instruments, Inc. (MKS), a publicly-traded company, and continues to hold 4.5 million shares at September 30, 2006. In the fourth quarter of 2006, the Company recorded a pretax gain of approximately $31 related to the divesture of the materials testing business. Also during the fourth quarter of 2006, the Company recorded a pretax charge of $14 related to the write-down of two businesses expected to be sold in early 2007 to their net realizable values. The Company also recorded a gain of approximately $18 in 2006 for payments received under the U.S. Continued Dumping and Subsidy Offset Act (Offset Act).

Gains, net for 2005 and 2004 include the following items. An approximate $13 gain from the sale of a manufacturing facility and an approximate $13 gain for a payment received under the Offset Act were recorded in 2005. In January 2004, the Company sold 2 million shares of MKS. The Company also sold its investment in the Louisville Ladder joint venture in 2004. The Company recorded a pretax gain of $27 in the second quarter of 2004 from these transactions.

(5) Rationalization of Operations

The change in the liability for the rationalization of operations during the years ended September 30 follows:

	2005	EXPENSE	ACQUISITIONS	PAID / UTILIZED	**2006**
Severance and benefits	$22	38	16	45	**31**
Lease/contract terminations	11	5	4	8	**12**
Fixed asset writedowns	–	2	–	2	**–**
Vacant facility and other shutdown costs	–	9	–	8	**1**
Start-up and moving costs	–	30	–	29	**1**
	$33	84	20	92	**45**

	2004	EXPENSE	PAID / UTILIZED	2005
Severance and benefits	$23	50	51	22
Lease/contract terminations	18	12	19	11
Fixed asset writedowns	–	3	3	–
Vacant facility and other shutdown costs	3	13	16	–
Start-up and moving costs	2	32	34	–
	$46	110	123	33

Rationalization of operations by segment is summarized as follows:

	2004	2005	**2006**
Process Management	$ 31	20	**14**
Industrial Automation	14	15	**12**
Network Power	26	35	**19**
Climate Technologies	17	15	**14**
Appliance and Tools	47	24	**25**
Corporate	(6)	1	**–**
Total	$129	110	**84**

Rationalization of operations comprises expenses associated with the Company's efforts to continuously improve operational efficiency and to expand globally in order to remain competitive on a worldwide basis. These expenses result from numerous individual actions implemented across the divisions on a routine basis and are not part of a large, company-wide program. Rationalization of operations includes ongoing costs for moving facilities, starting up plants from relocation as well as business expansion, exiting product lines, curtailing/downsizing operations due to changing economic conditions and other one-time items resulting from asset redeployment decisions. Shutdown costs include severance, benefits, stay bonuses, lease/contract terminations and asset writedowns. Start-up and moving costs include employee training and relocation, movement of assets and other items. Vacant facility costs include security, maintenance and utility costs associated with facilities that are no longer being utilized.

During 2006, rationalization of operations primarily related to the exit of approximately 10 production, distribution, or office facilities, including the elimination of approximately 1,700 positions, as well as costs related to facilities exited in previous periods. Noteworthy rationalization actions during 2006 are as follows. Process Management includes severance related to the shifting of certain regulator production from Western Europe to Eastern Europe. Industrial Automation includes start-up and moving costs related to shifting certain motor production in Western Europe to Eastern Europe, China and Mexico to leverage costs and remain competitive on a global basis. Network Power includes severance related to the closure of certain power conversion facilities acquired with Artesyn, severance, start-up and vacant facility costs related to the consolidation of certain power systems operations in North America and the consolidation of administrative operations in Europe to obtain operational synergies. Climate Technologies includes severance related to the movement of temperature sensors and controls production from Western Europe to China and start-up and moving costs related to a new plant in Eastern Europe in order to improve profitability. Appliance and Tools includes primarily severance and start-up and moving costs related to the shifting of certain tool and motor manufacturing operations from the United States and Western Europe to China and Mexico in order to consolidate facilities and improve profitability. The Company expects rationalization expense for 2007 to be approximately $100, including the costs to complete actions initiated before the end of 2006 and actions anticipated to be approved and initiated during 2007.

During 2005, rationalization of operations primarily related to the exit of approximately 25 production, distribution, or office facilities, including the elimination of approximately 2,100 positions, as well as costs related to facilities exited in previous periods. Noteworthy rationalization actions during 2005 are as follows. Process Management included severance and plant closure costs related to consolidation of instrumentation plants within Europe and consolidation of valve operations within North America, the movement of major distribution facilities to Asia, as well as several other cost reduction actions. Network Power included severance and lease termination costs related to certain power systems operations in Western Europe shifting to China and Eastern Europe in order to leverage product platforms and lower production and engineering costs to remain competitive on a global basis. This segment also included severance and start-up and moving costs related to the consolidation of North American power systems operations into the Marconi operations acquired in 2004. Appliance and Tools included severance, plant closure costs and start-up and moving costs related to consolidating

various industrial and hermetic motor manufacturing facilities for operational efficiency. Severance costs in this segment also related to shifting certain appliance control operations from the United States to Mexico and China in order to consolidate facilities and improve profitability.

During 2004, rationalization of operations primarily related to the exit of approximately 20 production, distribution, or office facilities, including the elimination of more than 2,000 positions, as well as costs related to facilities exited in previous periods. Rationalization actions during 2004 include the following. Process Management included severance and plant closure costs related to the closing of a valve plant due to consolidating operations within North America in response to weak market demand, severance costs related to the consolidation of European measurement operations in order to obtain operational synergies and several other reduction and consolidation actions. Network Power included severance and lease termination costs related to certain power systems operations in Western Europe shifting to China and Eastern Europe in order to leverage product platforms and lower production and engineering costs to remain competitive on a global basis. Climate Technologies included severance costs related to workforce reductions in the European temperature sensors and controls operations due to weakness in market demand. Appliance and Tools included severance and start-up and moving costs related to shifting certain motor manufacturing primarily from the United States to Mexico and China in order to consolidate facilities and improve profitability, and severance related to consolidating manufacturing operations in the professional tools business for operational efficiency.

(6) Goodwill and Other Intangibles

Acquisitions are accounted for under the purchase method, with substantially all goodwill assigned to the reporting unit that acquires the business. Under the annual impairment test, if a reporting unit's carrying amount exceeds its estimated fair value, a goodwill impairment is recognized to the extent that the reporting unit's carrying amount of goodwill exceeds the implied fair value of the goodwill. Fair values of reporting units are estimated using discounted cash flows and market multiples.

The change in goodwill by business segment follows:

	PROCESS MANAGEMENT	INDUSTRIAL AUTOMATION	NETWORK POWER	CLIMATE TECHNOLOGIES	APPLIANCE AND TOOLS	TOTAL
Balance, September 30, 2004	$1,638	880	1,770	380	591	5,259
Acquisitions	67	121	15		33	236
Foreign currency translation and other	(6)	(4)	(5)		(1)	(16)
Balance, September 30, 2005	$1,699	997	1,780	380	623	5,479
Acquisitions	58	27	351	25	20	481
Divestitures		(24)	(3)			(27)
Impairment			(5)			(5)
Foreign currency translation and other	21	16	39	3	6	85
Balance, September 30, 2006	**$1,778**	**1,016**	**2,162**	**408**	**649**	**6,013**

The gross carrying amount and accumulated amortization of intangibles (other than goodwill) by major class follow:

	GROSS CARRYING AMOUNT		ACCUMULATED AMORTIZATION		NET CARRYING AMOUNT	
	2005	**2006**	2005	**2006**	2005	**2006**
Intellectual property and customer relationships	$ 589	**794**	279	**324**	310	**470**
Capitalized software	600	**647**	443	**484**	157	**163**
	$1,189	**1,441**	722	**808**	467	**633**

Total intangible amortization expense for 2006, 2005 and 2004 was $107, $90 and $79, respectively. Based on intangible assets as of September 30, 2006, amortization expense will approximate $106 in 2007, $94 in 2008, $77 in 2009, $62 in 2010 and $59 in 2011.

(7) Financial Instruments

The Company selectively uses derivative financial instruments to manage interest costs, commodity prices and currency exchange risk. The Company does not hold derivatives for trading purposes. No credit loss is anticipated as the counterparties to these agreements are major financial institutions with high credit ratings.

To efficiently manage interest costs, the Company utilizes interest rate swaps as cash flow hedges of variable rate debt or fair value hedges of fixed rate debt. Also as part of its hedging strategy, the Company utilizes purchased option and forward exchange contracts and commodity swaps as cash flow or fair value hedges to minimize the impact of currency and commodity price fluctuations on transactions, cash flows, fair values and firm commitments. At September 30, 2006, substantially all of the contracts for the sale or purchase of European and other currencies and the purchase of copper and other commodities mature within two years; contracts with a fair value of approximately $130 mature in 2007.

Notional transaction amounts and fair values for the Company's outstanding derivatives, by risk category and instrument type, as of September 30, 2006 and 2005, are summarized as follows. Fair values of the derivatives do not consider the offsetting underlying hedged item.

	2005		**2006**	
	NOTIONAL AMOUNT	FAIR VALUE	**NOTIONAL AMOUNT**	**FAIR VALUE**
Foreign currency:				
Forwards	$1,202	18	**1,310**	**11**
Options	$ 81	6	**4**	**–**
Interest rate swaps	$ 114	(7)	**110**	**(4)**
Commodity contracts	$ 190	32	**457**	**130**

Fair values of the Company's financial instruments are estimated by reference to quoted prices from market sources and financial institutions, as well as other valuation techniques. The estimated fair value of long-term debt (including current maturities) exceeded the related carrying value by $40 and $119 at September 30, 2006 and 2005, respectively. The estimated fair value of each of the Company's other classes of financial instruments approximated the related carrying value at September 30, 2006 and 2005.

(8) Short-Term Borrowings and Lines of Credit

Short-term borrowings and current maturities of long-term debt are summarized as follows:

	2005	**2006**
Current maturities of long-term debt	$259	**2**
Commercial paper	114	**819**
Payable to banks	496	**28**
Other	101	**49**
Total	$970	**898**
Weighted-average short-term borrowing interest rate at year-end	4.0%	**4.9%**

In 2000, the Company issued 13 billion Japanese yen of commercial paper and simultaneously entered into a ten-year interest rate swap, which fixed the rate at 2.2 percent.

At year-end 2006, the Company maintained a five-year revolving credit facility effective until April 2011 amounting to $2.8 billion to support short-term borrowings and to assure availability of funds at prevailing interest rates. The credit facility does not contain any financial covenants and is not subject to termination based on a change in credit ratings or a material adverse change. There were no borrowings against U.S. lines of credit in the last three years.

(9) Long-Term Debt

Long-term debt is summarized as follows:

	2005	**2006**
6.3% notes due November 2005	$ 250	**–**
5 1/2% notes due September 2008	250	**250**
5% notes due October 2008	175	**175**
5.85% notes due March 2009	250	**250**
7 1/8% notes due August 2010	500	**500**
5.75% notes due November 2011	250	**250**
4.625% notes due October 2012	250	**250**
4 1/2% notes due May 2013	250	**250**
5 5/8% notes due November 2013	250	**250**
5% notes due December 2014	250	**250**
4.75% notes due October 2015	250	**250**
6% notes due August 2032	250	**250**
Other	212	**205**
	3,387	**3,130**
Less current maturities	259	**2**
Total	$3,128	**3,128**

During the fourth quarter of 2005, the Company issued $250 of 4.75%, ten-year notes under a shelf registration statement filed with the Securities and Exchange Commission. In 1999, the Company issued $250 of 5.85%, ten-year notes that were simultaneously swapped to U.S. commercial paper rates. The Company terminated the swap in 2001, establishing an effective interest rate of 5.7 percent. In 2000, the Company issued $600 of 7 7/8%, five-year notes that were simultaneously swapped to floating U.S. commercial paper rates. The Company terminated the swap in 2001, establishing an effective interest rate of 6.9 percent. During the first quarter of 2004, the Company swapped the $600 of 7 7/8% notes to a floating rate based on three-month LIBOR. The $600 of 7 7/8% notes and the swap matured in June 2005.

Long-term debt maturing during each of the four years after 2007 is $252, $474, $600 and $37, respectively. Total interest paid related to short-term borrowings and long-term debt was approximately $214, $247 and $233 in 2006, 2005 and 2004, respectively.

As of September 30, 2006, the Company could issue up to $2.25 billion in debt securities, preferred stock, common stock, warrants, share purchase contracts and share purchase units under the shelf registration statement filed with the Securities and Exchange Commission. The Company may sell securities in one or more separate offerings with the size, price and terms to be determined at the time of sale. The net proceeds from the sale of the securities will be used for general corporate purposes, which may include, but are not limited to, working capital, capital expenditures, financing acquisitions and the repayment of short- or long-term borrowings. The net proceeds may be invested temporarily until they are used for their stated purpose.

(10) Retirement Plans

Retirement plan expense includes the following components:

	U.S. PLANS			NON-U.S. PLANS		
	2004	2005	**2006**	2004	2005	**2006**
Defined benefit plans:						
Service cost (benefits earned during the period)	$ 49	48	**58**	15	14	**19**
Interest cost	136	145	**145**	27	31	**32**
Expected return on plan assets	(196)	(207)	**(202)**	(21)	(27)	**(32)**
Net amortization	65	64	**100**	14	13	**16**
Net periodic pension expense	54	50	**101**	35	31	**35**
Defined contribution and multiemployer plans	66	69	**85**	22	23	**25**
Total retirement plan expense	$ 120	119	**186**	57	54	**60**

The reconciliations of the actuarial present value of the projected benefit obligations and of the fair value of plan assets for defined benefit pension plans follow:

	U.S. PLANS		NON-U.S. PLANS	
	2005	**2006**	2005	**2006**
Projected benefit obligation, beginning	$2,330	**2,747**	607	**707**
Service cost	48	**58**	14	**19**
Interest cost	145	**145**	31	**32**
Actuarial loss (gain)	320	**(386)**	101	**(53)**
Benefits paid	(118)	**(122)**	(27)	**(29)**
Acquisitions/divestitures, net	19	**17**	–	**24**
Foreign currency translation and other	3	**5**	(19)	**11**
Projected benefit obligation, ending	$2,747	**2,464**	707	**711**
Fair value of plan assets, beginning	$2,292	**2,566**	433	**492**
Actual return on plan assets	258	**233**	47	**37**
Employer contributions	122	**91**	52	**33**
Benefits paid	(118)	**(122)**	(27)	**(29)**
Acquisitions/divestitures, net	10	**16**	–	**18**
Foreign currency translation and other	2	**1**	(13)	**4**
Fair value of plan assets, ending	$2,566	**2,785**	492	**555**
Plan assets in excess of (less than) benefit obligation as of June 30	$ (181)	**321**	(215)	**(156)**
Unrecognized net loss	1,079	**564**	240	**179**
Unrecognized prior service cost (benefit)	9	**10**	(3)	**(2)**
Adjustment for fourth quarter contributions	1	**1**	1	**1**
Net amount recognized in the balance sheet	$ 908	**896**	23	**22**
Accumulated benefit obligation	$2,535	**2,344**	595	**612**

	U.S. PLANS			NON-U.S. PLANS		
	2004	2005	**2006**	2004	2005	**2006**
Weighted-average assumptions used to determine net pension expense:						
Discount rate	6.00%	6.25%	**5.25%**	5.2%	5.4%	**4.7%**
Expected return on plan assets	8.50%	8.50%	**8.00%**	7.2%	7.4%	**7.2%**
Rate of compensation increase	3.25%	3.25%	**3.00%**	3.3%	3.1%	**3.0%**
Weighted-average assumptions used to determine benefit obligations as of June 30:						
Discount rate	6.25%	5.25%	**6.50%**	5.4%	4.7%	**4.9%**
Rate of compensation increase	3.25%	3.00%	**3.25%**	3.1%	3.0%	**3.1%**

At September 30, 2006 and 2005, the pension assets recognized in the balance sheet were $1,037 and $925, and the pension liabilities recognized in the balance sheet were $208 and $276, respectively; in addition, $89 and $282 were included in accumulated other comprehensive income at September 30, 2006 and 2005, respectively. As of the plans' June 30 measurement date, the projected benefit obligation, accumulated benefit obligation, and fair value of plan assets for the retirement plans with accumulated benefit obligations in excess of plan assets were $623, $570 and $360, respectively, for 2006, and $1,006, $938 and $656, respectively, for 2005.

Effective for 2007, the discount rate for the U.S. retirement plans was adjusted to 6.5 percent based on the changes in market interest rates. Defined benefit pension plan expense is expected to decrease approximately $20 in 2007. In September 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 158 (FAS 158). The Company is analyzing the impact of adopting FAS 158 and estimates that if the provisions of FAS 158 were applied as of September 30, 2006, an after-tax charge to equity of approximately $500 ($800 pretax) would have been reported.

The primary objective for the investment of plan assets is to secure participant retirement benefits, while earning a reasonable rate of return. Plan assets are invested consistent with the provisions of prudence and diversification rules of ERISA and with a long-term investment horizon. The expected return on plan assets assumption is determined by reviewing the investment return of the plans for the past ten years and the historical return (since 1926) of an asset mix approximating Emerson's current asset allocation targets and evaluating these returns in relation to expectations of various investment organizations to determine whether long-term future returns are expected to differ significantly from the past. The Company's pension plan asset allocations at June 30, 2006 and 2005, and target weighted-average allocations are as follows:

	U.S. PLANS			NON-U.S. PLANS		
	2005	**2006**	TARGET	2005	**2006**	TARGET
Asset category						
Equity securities	69%	**68%**	66 - 70%	56%	**55%**	50 - 60%
Debt securities	27%	**28%**	26 - 32%	37%	**36%**	30 - 40%
Other	4%	**4%**	2 - 5%	7%	**9%**	5 - 10%
	100%	**100%**	100%	100%	**100%**	100%

The Company estimates that future benefit payments for the U.S. plans will be as follows: $126 in 2007, $132 in 2008, $138 in 2009, $145 in 2010, $152 in 2011 and $881 in total over the five years 2012 through 2016. Using foreign exchange rates as of September 30, 2006, the Company estimates that future benefit payments for the non-U.S. plans will be as follows: $24 in 2007, $26 in 2008, $27 in 2009, $29 in 2010, $31 in 2011 and $190 in total over the five years 2012 through 2016. In 2007, the Company expects to contribute approximately $100 to $150 to the retirement plans.

(11) Postretirement Plans

The Company sponsors unfunded postretirement benefit plans (primarily health care) for U.S. retirees and their dependents. Net postretirement plan expense for the years ended September 30 follows:

	2004	2005	**2006**
Service cost	$ 5	6	**5**
Interest cost	25	27	**26**
Net amortization	19	21	**32**
Net postretirement plan expense	$49	54	**63**

The reconciliations of the actuarial present value of accumulated postretirement benefit obligations follow:

	2005	**2006**
Benefit obligation, beginning	$ 444	**502**
Service cost	6	**5**
Interest cost	27	**26**
Actuarial loss	55	**16**
Benefits paid	(43)	**(39)**
Acquisitions/divestitures and other	13	**6**
Benefit obligation, ending	502	**516**
Unrecognized net loss	(134)	**(102)**
Unrecognized prior service benefit	7	**6**
Postretirement benefit liability recognized in the balance sheet	$ 375	**420**

The assumed discount rates used in measuring the obligations as of September 30, 2006, 2005 and 2004, were 5.75 percent, 5.25 percent and 5.75 percent, respectively. The assumed health care cost trend rate for 2007 was 10.0 percent, declining to 5.0 percent in the year 2016. The assumed health care cost trend rate for 2006 was 9.5 percent, declining to 5.0 percent in the year 2014. A one-percentage-point increase or decrease in the assumed health care cost trend rate for each year would increase or decrease the obligation as of September 30, 2006 and the 2006 postretirement plan expense by less than 5 percent. The Company estimates that future benefit payments will be as follows: $44 in 2007, $45 in 2008, $46 in 2009, $47 in 2010, $53 in 2011 and $241 in total over the five years 2012 through 2016.

(12) Contingent Liabilities and Commitments

Emerson is a party to a number of pending legal proceedings and claims, including those involving general and product liability and other matters, several of which claim substantial amounts of damages. The Company accrues for such liabilities when it is probable that future costs (including legal fees and expenses) will be incurred and such costs can be reasonably estimated. Such accruals are based on developments to date, management's estimates of the outcomes of these matters, the Company's experience in contesting, litigating and settling other similar matters, and any related insurance coverage.

Although it is not possible to predict the ultimate outcome of the matters discussed above, historically, the Company has been successful in defending itself against claims and suits that have been brought against it. The Company will continue to defend itself vigorously in all such matters. While the Company believes a material adverse impact is unlikely, given the inherent uncertainty of litigation, a remote possibility exists that a future adverse development could have a material adverse impact on the Company.

The Company enters into indemnification agreements in the ordinary course of business in which the indemnified party is held harmless and is reimbursed for losses incurred from claims by third parties. In connection with divestitures of certain assets or businesses, the Company often provides indemnities to the buyer with respect to certain matters including, for example, environmental liabilities and unidentified tax liabilities related to periods prior to the disposition. Due to the uncertain nature of the indemnities, the maximum liability cannot be quantified. Liabilities for obligations are recorded when probable and when they can be reasonably estimated. Historically, the Company has not made significant payments for these obligations.

At September 30, 2006, there were no known contingent liabilities (including guarantees, pending litigation, taxes and other claims) that management believes will be material in relation to the Company's financial statements, nor were there any material commitments outside the normal course of business.

(13) Income Taxes

Earnings before income taxes consist of the following:

	2004	2005	**2006**
United States	$1,022	1,157	**1,518**
Non-U.S.	830	992	**1,166**
Earnings before income taxes	$1,852	2,149	**2,684**

The principal components of income tax expense follow:

	2004	2005	**2006**
Current:			
Federal	$132	458	**394**
State and local	26	42	**57**
Non-U.S.	229	272	**316**
Deferred:			
Federal	185	(41)	**73**
State and local	5	(7)	**8**
Non-U.S.	18	3	**(9)**
Income tax expense	$595	727	**839**

The federal corporate statutory rate is reconciled to the Company's effective income tax rate as follows:

	2004	2005	2006
Federal corporate statutory rate	35.0%	35.0%	**35.0%**
State and local taxes, less federal tax benefit	1.1	1.0	**1.6**
Non-U.S. rate differential	(2.1)	(3.2)	**(3.4)**
Non-U.S. tax holidays	(1.7)	(1.6)	**(1.6)**
Export benefit	(1.4)	(1.1)	**(0.8)**
U.S. manufacturing deduction	–	–	**(0.4)**
Repatriation - American Jobs Creation Act	–	3.0	**–**
Other	1.2	0.7	**0.9**
Effective income tax rate	32.1%	33.8%	**31.3%**

Non-U.S. tax holidays reduce the tax rate in certain foreign jurisdictions, the majority of which expire over the next five years. The American Jobs Creation Act of 2004 (the Act) was signed into law on October 22, 2004. The Act allows the repatriation of foreign earnings at a reduced rate for one year, subject to certain limitations. During 2005, the Company repatriated approximately $1.4 billion ($1.8 billion in total) of cash from undistributed earnings of non-U.S. subsidiaries under the Act. As a result, the Company recorded a tax expense of $63, or $0.15 per share, in 2005.

The principal items that gave rise to deferred income tax assets and liabilities follow:

	2005	2006
Deferred tax assets:		
Accrued liabilities	$ 176	**218**
Postretirement and postemployment benefits	153	**160**
Employee compensation and benefits	149	**124**
NOL and tax credits	256	**254**
Capital loss benefit	72	**30**
Other	141	**126**
Total	$ 947	**912**
Valuation allowance	$ (137)	**(183)**
Deferred tax liabilities:		
Property, plant and equipment	$ (295)	**(316)**
Leveraged leases	(117)	**(110)**
Pension	(245)	**(308)**
Intangibles	(267)	**(346)**
Other	(82)	**(42)**
Total	$(1,006)	**(1,122)**
Net deferred income tax liability	$ (196)	**(393)**

At September 30, 2006 and 2005, respectively, net current deferred tax assets were $269 and $315, and net noncurrent deferred tax liabilities were $662 and $511. Total income taxes paid were approximately $820, $600 and $380 (net of the capital loss benefit received of $140) in 2006, 2005 and 2004, respectively. A majority of the $30 capital loss carryforward can be utilized through 2008. The majority of the $231 net operating losses can be carried forward indefinitely, while the remainders expire over varying periods. In addition, a majority of the $23 of tax credits can be carried forward through 2015. The valuation allowance for deferred tax assets at September 30, 2006, includes $55 related to acquisitions, which would reduce goodwill if the deferred tax assets are ultimately realized.

(14) Stock-Based Compensation

The Company's stock-based compensation plans include stock options and incentive shares.

STOCK OPTIONS

The Company's Stock Option Plans permit key officers and employees to purchase common stock at specified prices. Options are granted at 100 percent of the market value of the Company's common stock on the date of grant, generally vest one-third each year and expire ten years from the date of grant. Compensation cost is recognized over the vesting period based on the number of options expected to vest. At September 30, 2006, approximately 7.8 million options remained available for grant under these plans.

Changes in shares subject to option during the year ended September 30, 2006, follow:

(SHARES IN THOUSANDS)	AVERAGE EXERCISE PRICE PER SHARE	SHARES	TOTAL INTRINSIC VALUE OF AWARDS	AVERAGE REMAINING CONTRACTUAL LIFE
Beginning of year	$54.44	9,859		
Options granted	$75.59	585		
Options exercised	$49.94	(2,434)		
Options canceled	$63.38	(106)		
End of year	$57.27	7,904	$210	5.3 years
Exercisable at year-end	$54.04	5,876	$175	4.3 years

The weighted-average grant-date fair value per share of options granted was $17.59, $12.77 and $11.13 for 2006, 2005 and 2004, respectively. The total intrinsic value of options exercised was $74, $26 and $22 in 2006, 2005 and 2004, respectively. Cash received from option exercises under share option plans was $89, $50 and $37 and the actual tax benefit realized for the tax deductions from option exercises was $6, $4 and $2 for 2006, 2005 and 2004, respectively.

The fair value of each award is estimated on the grant date using the Black-Scholes option-pricing model. Weighted-average assumptions used in the Black-Scholes valuations for 2006, 2005 and 2004 are as follows: risk-free interest rate based on the U.S. Treasury yield of 4.4 percent, 3.5 percent and 3.1 percent, dividend yield of 2.4 percent, 2.5 percent and 2.8 percent and expected volatility based on historical volatility of 23 percent, 24 percent and 25 percent for 2006, 2005 and 2004, respectively. The expected life of an option is based on historical experience and expected exercise patterns in the future. Expected lives were 6 years, 5 years and 5 years for 2006, 2005 and 2004, respectively.

INCENTIVE SHARES

The Company's Incentive Shares Plans include performance share awards, which involve the distribution of common stock to key management personnel subject to certain conditions and restrictions. Compensation cost is recognized over the service period based on the number of shares expected to be ultimately issued. Performance share awards are accounted for as liabilities in accordance with FAS 123R. Compensation expense is adjusted at the end of each period to reflect the change in the fair value of the awards.

In 2006, as a result of the Company achieving certain performance objectives at the end of 2005, 1,044,995 rights to receive common shares vested and were distributed to participants as follows: 472,739 issued in shares, 345,987 withheld for income taxes, 205,043 paid in cash and 21,226 deferred by participants for future distribution. As of September 30, 2006, 2,364,630 rights to receive common shares (awarded primarily in 2004) were outstanding, which are contingent upon accomplishing certain Company performance objectives by 2007 and the performance of services by the employees.

The Company's Incentive Shares Plans also include restricted stock awards, which involve the distribution of the Company's common stock to key management personnel subject to service periods ranging from three to ten years. The fair value of these awards is determined by the market price of the Company's stock at the date of grant. Compensation cost is recognized over the applicable service period. In 2006, 724,654 shares of restricted stock vested as a result of the fulfillment of the applicable service periods and were distributed to participants as follows: 500,887 issued in shares and 223,767 withheld for income taxes. As of September 30, 2006, there were 1,033,777 shares of restricted stock awards outstanding.

Changes in awards outstanding but not yet earned under the Incentive Shares Plans during the year ended September 30, 2006, follow:

(SHARES IN THOUSANDS)	SHARES	AVERAGE GRANT DATE FAIR VALUE PER SHARE
Beginning of year	5,027	$63.16
Granted	233	$73.46
Earned/vested	(1,770)	$65.88
Canceled	(92)	$63.16
End of year	3,398	$62.45

The total fair value of shares earned/vested was $123, $5 and $24 under the Incentive Shares Plans of which $55, $2 and $9 was paid in cash, primarily for tax withholding, in 2006, 2005 and 2004, respectively. As of September 30, 2006, approximately 10.7 million shares remained available for award under the Incentive Shares Plans.

In addition to the stock option and incentive share plans, the Company issued 11,882 shares of restricted stock in 2006 under the Restricted Stock Plan for Non-Management Directors and 0.2 million shares remained available for issuance as of September 30, 2006.

Compensation cost for the stock option and incentive share plans was $81, $100 and $66, for 2006, 2005 and 2004, respectively. Total income tax benefit recognized in the income statement for these compensation arrangements during 2006, 2005 and 2004 were $22, $33 and $22, respectively. As of September 30, 2006, there was $113 of total unrecognized compensation cost related to nonvested awards granted under these plans, which is expected to be recognized over a weighted-average period of 1.7 years.

(15) Common Stock

At September 30, 2006, 28,976,471 shares of common stock were reserved, primarily for issuance under the Company's stock-based compensation plans. During 2006, 10,725,600 treasury shares were acquired and 2,420,935 treasury shares were issued.

Approximately 1.2 million preferred shares are reserved for issuance under a Preferred Stock Purchase Rights Plan. Under certain conditions involving the acquisition of or an offer for 20 percent or more of the Company's common stock, all holders of Rights, except an acquiring entity, would be entitled (i) to purchase, at an exercise price of $260, common stock of the Company or an acquiring entity with a value twice the exercise price, or (ii) at the option of the Board, to exchange each Right for one share of common stock. The Rights remain in existence until November 1, 2008, unless earlier redeemed (at one-half cent per Right), exercised, or exchanged under the terms of the plan.

(16) Business Segment Information

The Company designs and supplies product technology and delivers engineering services in a wide range of industrial, commercial and consumer markets around the world. The divisions of the Company are organized primarily by the nature of the products and services provided. The Process Management segment includes systems and software, measurement and analytical instrumentation, valves, actuators and regulators, and services and solutions for automated industrial processes. The Industrial Automation segment includes industrial motors and drives, power transmission equipment, alternators, materials joining and precision cleaning, fluid power and control, and electrical distribution equipment. The Network Power segment consists of uninterruptible power supplies, power conditioning and electrical switching equipment, and precision cooling and site monitoring systems. The Climate Technologies segment consists of compressors, temperature sensors and controls, thermostats, flow controls, and remote monitoring services. The Appliance and Tools segment includes general and special purpose motors and controls, appliances and appliance components, plumbing tools, and storage products.

The primary income measure used for assessing performance and making operating decisions is earnings before interest and income taxes. Intersegment sales approximate market prices. Accounting method differences between segment reporting and the consolidated financial statements include primarily management fees allocated to segments based on a percentage of sales and the accounting for pension and other retirement plans. Gains and losses from divestitures of businesses are included in Corporate and other. Corporate assets include primarily cash and equivalents, investments, pensions, deferred charges, and certain fixed assets.

Summarized information about the Company's operations by business segment and by geographic area follows:

BUSINESS SEGMENTS

(See Notes 3, 4, 5 and 6)

	SALES			EARNINGS			TOTAL ASSETS		
	2004	2005	**2006**	2004	2005	**2006**	2004	2005	**2006**
Process Management	$ 3,703	4,200	**4,875**	476	671	**878**	3,634	3,894	**4,146**
Industrial Automation	2,936	3,242	**3,767**	391	464	**569**	2,503	2,698	**2,941**
Network Power	2,692	3,317	**4,350**	297	373	**484**	3,234	3,379	**4,436**
Climate Technologies	2,983	3,041	**3,424**	467	453	**523**	1,887	1,956	**2,129**
Appliance and Tools	3,749	4,008	**4,313**	530	534	**550**	2,440	2,526	**2,670**
	16,063	17,808	**20,729**	2,161	2,495	**3,004**	13,698	14,453	**16,322**
Differences in accounting methods				126	145	**176**			
Corporate and other (a)				(225)	(282)	**(289)**	2,663	2,774	**2,350**
Sales eliminations / Interest	(448)	(503)	**(596)**	(210)	(209)	**(207)**			
Total	$15,615	17,305	**20,133**	1,852	2,149	**2,684**	16,361	17,227	**18,672**

(a) Corporate and other increased from 2004 to 2005 due to higher incentive compensation cost and other items (see Note 14).

	INTERSEGMENT SALES			DEPRECIATION AND AMORTIZATION EXPENSE			CAPITAL EXPENDITURES		
	2004	2005	**2006**	2004	2005	**2006**	2004	2005	**2006**
Process Management	$ 3	2	**3**	117	125	**128**	75	89	**101**
Industrial Automation	14	19	**21**	96	95	**100**	67	68	**87**
Network Power	9	9	**10**	70	76	**98**	36	55	**103**
Climate Technologies	32	37	**43**	120	118	**127**	94	148	**148**
Appliance and Tools	390	436	**519**	141	134	**137**	108	136	**149**
Corporate and other				13	14	**17**	20	22	**13**
Total	$448	503	**596**	557	562	**607**	400	518	**601**

GEOGRAPHIC

	SALES BY DESTINATION			PROPERTY, PLANT AND EQUIPMENT		
	2004	2005	**2006**	2004	2005	**2006**
United States	$ 8,262	9,126	**10,588**	1,880	1,919	**1,963**
Europe	3,649	3,890	**4,334**	539	511	**583**
Asia	2,085	2,370	**2,920**	307	343	**419**
Latin America	533	670	**857**	135	149	**177**
Other regions	1,086	1,249	**1,434**	76	81	**78**
Total	$15,615	17,305	**20,133**	2,937	3,003	**3,220**

(17) Other Financial Data

Items reported in earnings during the years ended September 30 include the following:

	2004	2005	**2006**
Depreciation	$478	472	**500**
Research and development	$280	303	**356**
Rent expense	$233	241	**263**

The Company leases computers, transportation equipment and various other property under operating lease agreements. The minimum annual rentals under noncancelable long-term leases, exclusive of maintenance, taxes, insurance and other operating costs, will approximate $143 in 2007, $104 in 2008, $70 in 2009, $46 in 2010 and $43 in 2011.

Other assets, other are summarized as follows:

	2005	**2006**
Pension plans	$ 925	**1,037**
Intellectual property and customer relationships	310	**470**
Equity and other investments	248	**171**
Capitalized software	157	**163**
Leveraged leases	116	**109**
Other	152	**159**
Total	$1,908	**2,109**

Items reported in accrued expenses include the following:

	2005	**2006**
Employee compensation	$ 445	**518**
Product warranty	$ 174	**206**

Other liabilities are summarized as follows:

	2005	**2006**
Deferred income taxes	$ 567	**724**
Postretirement plans, excluding current portion	325	**371**
Retirement plans	336	**253**
Minority interest	142	**176**
Other	398	**492**
Total	$1,768	**2,016**

(18) Quarterly Financial Information (Unaudited)

	First Quarter		Second Quarter		Third Quarter		Fourth Quarter		Fiscal Year	
	2005	**2006**	2005	**2006**	2005	**2006**	2005	**2006**	2005	**2006**
Net sales	$3,970	**4,548**	4,227	**4,852**	4,465	**5,217**	4,643	**5,516**	17,305	**20,133**
Gross profit	$1,412	**1,593**	1,502	**1,734**	1,600	**1,856**	1,669	**1,985**	6,183	**7,168**
Net earnings	$ 297	**399**	348	**434**	358	**486**	419	**526**	1,422	**1,845**
Earnings per common share:										
Basic	$ 0.71	**0.97**	0.84	**1.06**	0.86	**1.19**	1.02	**1.30**	3.43	**4.52**
Diluted	$ 0.70	**0.96**	0.83	**1.05**	0.86	**1.18**	1.01	**1.29**	3.40	**4.48**
Dividends per common share	$0.415	**0.445**	0.415	**0.445**	0.415	**0.445**	0.415	**0.445**	1.66	**1.78**
Common stock prices:										
High	$70.88	**77.40**	70.20	**85.67**	68.61	**87.47**	72.04	**84.06**	72.04	**87.47**
Low	$61.22	**67.93**	63.93	**75.08**	60.69	**78.62**	61.47	**76.15**	60.69	**67.93**

See Notes 3 and 4 for information regarding the Company's acquisition and divestiture activities and non-recurring items.

Emerson Electric Co. common stock (symbol EMR) is listed on the New York Stock Exchange and the Chicago Stock Exchange.

(19) Subsequent Event

In November 2006, the Company's Board of Directors declared a two-for-one split of the Company's common stock, effected in the form of a 100 percent stock dividend, to shareholders of record as of November 17, 2006, with a distribution date of December 11, 2006 (shares begin trading on a post-split basis on December 12, 2006). This stock split will result in the issuance of approximately 476.7 million additional shares of common stock and will be accounted for by the transfer of approximately $238 from additional paid-in capital and retained earnings to common stock. Pro forma earnings per share amounts on a post-split basis for the years ended September 30, 2006, 2005 and 2004 would be as follows:

	2004	2005	**2006**
Earnings per common share			
Basic:			
As reported	$3.00	3.43	**4.52**
Post-split	$1.50	1.71	**2.26**
Diluted:			
As reported	$2.98	3.40	**4.48**
Post-split	$1.49	1.70	**2.24**

Information presented in the Consolidated Financial Statements, related notes and Eleven-Year Summary have not been restated to reflect the two-for-one stock split.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Emerson Electric Co.:

We have audited the accompanying consolidated balance sheets of Emerson Electric Co. and subsidiaries as of September 30, 2006 and 2005, and the related consolidated statements of earnings, stockholders' equity, and cash flows for each of the years in the three-year period ended September 30, 2006. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Emerson Electric Co. and subsidiaries as of September 30, 2006 and 2005, and the results of their operations and their cash flows for each of the years in the three-year period ended September 30, 2006, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Emerson Electric Co.'s internal control over financial reporting as of September 30, 2006, based on criteria established in *Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission* (COSO), and our report dated November 20, 2006 expressed an unqualified opinion on management's assessment of, and the effective operation of, internal control over financial reporting.

KPMG LLP

St. Louis, Missouri

November 20, 2006

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Emerson Electric Co.:

We have audited management's assessment, included in the accompanying Management's Report on Internal Control Over Financial Reporting, that Emerson Electric Co. maintained effective internal control over financial reporting as of September 30, 2006, based on criteria established in *Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission* (COSO). Emerson Electric Co.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that Emerson Electric Co. maintained effective internal control over financial reporting as of September 30, 2006, is fairly stated, in all material respects, based on criteria established in *Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission* (COSO). Also, in our opinion, Emerson Electric Co. maintained, in all material respects, effective internal control over financial reporting as of September 30, 2006, based on criteria established in *Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission* (COSO).

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Emerson Electric Co. and subsidiaries as of September 30, 2006 and 2005, and the related consolidated statements of earnings, stockholders' equity, and cash flows for each of the years in the three-year period ended September 30, 2006, and our report dated November 20, 2006 expressed an unqualified opinion on those consolidated financial statements.

KPMG LLP

St. Louis, Missouri

November 20, 2006

Eleven-Year Summary

EMERSON ELECTRIC CO. & SUBSIDIARIES

Years ended September 30 | Dollars in millions, except per share amounts

		2006	2005	2004
Summary of Operations	Net sales	**$20,133**	17,305	15,615
	Gross profit	**$ 7,168**	6,183	5,566
	Interest expense	**$ 225**	243	234
	Earnings from continuing operations	**$ 1,845**	1,422[a]	1,257
	Percent of net sales	**9.2%**	8.2%	8.1%
	Net earnings	**$ 1,845**	1,422[a]	1,257
	Operating cash flow	**$ 2,512**	2,187	2,216
	Return on average stockholders' equity	**23.7%**	19.4%	18.4%
Per Share of Common Stock	Diluted:			
	Earnings from continuing operations	**$ 4.48**	3.40[a]	2.98
	Net earnings	**$ 4.48**	3.40[a]	2.98
	Cash dividends	**$ 1.78**	1.66	1.60
	Book value	**$ 20.27**	18.02	17.26
Year-End Financial Position	Operating working capital	**$ 2,044**	1,643	1,633
	Percent of net sales	**10.1%**	9.5%	10.5%
	Property, plant and equipment, net	**$ 3,220**	3,003	2,937
	Total assets	**$18,672**	17,227	16,361
	Long-term debt	**$ 3,128**	3,128	3,136
	Stockholders' equity	**$ 8,154**	7,400	7,238
	Total debt to total capital	**33.1%**	35.6%	35.8%
	Net debt to net capital	**28.1%**	27.7%	27.0%
Other Data	Capital expenditures	**$ 601**	518	400
	Depreciation	**$ 500**	472	478
	Total taxes, including income taxes	**$ 1,362**	1,227	1,044
	Salaries and wages	**$ 3,751**	3,161	3,320
	Average number of employees	**127,800**	114,200	107,800
	Approximate number of stockholders of record at year-end	**27,065**	28,780	30,200
	Average common shares – diluted (in thousands)	**412,238**	418,860	422,195

Note: All share and per share data reflect the 1997 two-for-one stock split.

See Note 3 for information regarding the Company's acquisition and divestiture activities.

The operating results of Dura-Line are classified as discontinued operations for 2000-2003.

(a) Includes a tax expense of $63 ($0.15 per share) related to the one-time opportunity to repatriate foreign earnings under the American Jobs Creaton Act of 2004.

(b) Includes the cumulative effect of a change in accounting principle of $938 ($2.23 per share).

(c) Before change in accounting principle.

(d) Includes a $377 charge ($260 after-tax, or $0.61 per share), of which $358 ($248 after-tax, or $0.58 per share) was reported in continuing operations, primarily for the disposition of facilities and exiting of product lines.

2003	2002	2001	2000	1999	1998	1997	1996
13,958	13,748	15,311	15,351	14,270	13,447	12,299	11,150
4,898	4,809	5,324	5,473	5,076	4,852	4,433	3,985
246	250	304	288	190	152	121	127
1,013	1,076	1,049(d)	1,409	1,314	1,229	1,122	1,019
7.3%	7.8%	6.8%	9.2%	9.2%	9.1%	9.1%	9.1%
1,089	122(b)	1,032(d)	1,422	1,314	1,229	1,122	1,019
1,731	1,818	1,708	1,840	1,811	1,652	1,499	1,317
17.9%	17.9%(c)	16.5%	22.6%	21.9%	21.9%	20.8%	19.9%
2.41	2.56	2.44(d)	3.27	3.00	2.77	2.50	2.25
2.59	0.29(b)	2.40(d)	3.30	3.00	2.77	2.50	2.25
1.57	1.55	1.53	1.43	1.30	1.18	1.08	0.98
15.34	13.65	14.57	14.98	14.27	13.24	12.30	11.96
1,778	1,741	2,033	2,336	2,222	2,294	2,098	1,984
12.7%	12.6%	13.1%	15.0%	15.6%	17.1%	17.1%	17.8%
2,962	3,116	3,288	3,243	3,154	3,012	2,735	2,451
15,194	14,545	15,046	15,164	13,624	12,660	11,463	10,481
3,733	2,990	2,256	2,248	1,317	1,057	571	773
6,460	5,741	6,114	6,403	6,181	5,803	5,421	5,353
39.0%	44.2%	43.5%	41.8%	34.6%	30.8%	27.1%	24.5%
34.5%	42.0%	41.5%	40.2%	32.7%	29.0%	24.9%	22.9%
337	384	554	692	592	603	575	514
463	457	462	454	447	406	369	339
843	915	982	1,196	1,126	1,093	1,034	963
3,153	3,107	3,389	3,376	3,171	3,003	2,771	2,569
106,700	111,500	124,500	123,400	116,900	111,800	100,700	86,400
31,800	32,700	33,700	35,000	36,300	37,200	35,900	29,800
420,918	420,891	429,452	431,395	438,397	444,121	449,501	452,754

Board of Directors

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Companies, Inc.

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St. Louis, Missouri
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Officer, and President

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Stores Company

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Gerald A. Lodge
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Innocal Venture Firms

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Executive Vice President

J.J. Lindemann
Executive Vice President

E.L. Monser
Chief Operating Officer

J-P.L. Montupet
Executive Vice President

P.J. Sly
Executive Vice President

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A.A. Busch III
D.C. Farrell
R.B. Horton
G.A. Lodge
V.R. Loucks Jr.

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R.L. Ridgway

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C. Fernandez G.
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Pension Committee
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A.F. Golden
R.B. Horton
J.B. Menzer
J.W. Prueher

Management

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Chairman, Chief Executive Officer, and President

W.J. Galvin
Senior Executive Vice President and Chief Financial Officer

E.L. Monser
Chief Operating Officer

C.A. Peters
Senior Executive Vice President

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J.M. Berra
Executive Vice President

T.E. Bettcher
Executive Vice President

J.J. Lindemann
Executive Vice President

J-P.L. Montupet
Executive Vice President

P.J. Sly
Executive Vice President

E.K. Feeney
Senior Vice President

R.P. Bauer
Group Vice President

J.L. Geldmacher
Group Vice President

C. Henry
Group Vice President

P.K. Murphy
Group Vice President

E.M. Purvis
Group Vice President

R.J. Schul
Group Vice President

E.M. Shanahan
Group Vice President

J-P.D. Yaouanc
Group Vice President

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Senior Vice President-
Planning and Development

J.L. Bansch
Vice President -
Benefits

L.C. Barrett
President-
Emerson Canada

C.T. Bauer
Vice President and Associate General Counsel

R.E. Browning
Vice President-
Development

F.K. Burdell III
Vice President-
Shared Services

K. Button Bell
Vice President and Chief Marketing Officer

J.R. Carius
Vice President and Chief Employment Counsel

R.M. Cox Jr.
Senior Vice President-
Administration

F.J. Dellaquila
Senior Vice President-
Acquisitions and Development

C.A. Doiron
Vice President-
Supply Chain

B.N. Eckhardt
Senior Vice President and Controller

L.A. Flavin
Vice President-
Audit

G.A. Fromknecht
Vice President-
Global Logistics

K.D. Hahn
Vice President-
Information Technology

S.C. Hassell
Vice President and Chief Information Officer

C.G. Heath
Vice President-
Executive Compensation

P.A. Hutchison
Senior Vice President-
Human Resources

R.E. Keefe
Vice President-
Manufacturing

D.A. Kubly
Vice President and Associate General Counsel

H.J. Lamboley Jr.
Vice President-
Environmental Affairs and Real Estate

A.E. Lebon
Vice President-
Labor Relations

R.D. Ledford
Senior Vice President and Chief Technology Officer

R.M. Levy
Vice President-
Development

R.D. McDonald
Vice President-
Government Affairs

P.E. McKnight
Senior Vice President-
Organization Planning

M.J. Molloy
Vice President-
Development

D.C. Moon
Vice President-
Tax

S.J. Pelch
Vice President-
Planning

D.J. Rabe
Vice President and Treasurer

L.A. Rodriguez
President-
Emerson Latin America

S.C. Roemer
Vice President-
Financial Planning

M.G. Rohret
Vice President-
Employee Relations

R.J. Schlueter
Vice President and Chief Accounting Officer

P. Sen
President-
Emerson India

D.D. Sollberger
Vice President-
Global Procurement

C.J. Stephen
Vice President-
Project Management Organization

J.D. Switzer
Senior Vice President-
Development

C.L. Tucker
Assistant Treasurer and Director-
Investor Relations

S.E. Von Gruben
Vice President-
Aviation

B.J. Walsh
Vice President and Associate General Counsel

T.G. Westman
Vice President and Associate General Counsel

W.W. Withers
Executive Vice President, Secretary and General Counsel

P.K. Yam
President-
Emerson Greater China

Stockholders Information

STOCKHOLDER INQUIRIES AND SERVICES

Inquiries regarding dividend payments, loss, or nonreceipt of a dividend check, stock transfers (including name changes, gifts, and inheritances), lost stock certificates, Form 1099 information, and address changes should be directed to the Registrar and Transfer Agent.

REGISTRAR AND TRANSFER AGENT

By Mail:
Mellon Investor Services
Attention: Emerson Electric Co.
P.O. Box 3316
South Hackensack, NJ 07606

By Phone:
Toll-Free: (888) 213-0970
TDD for Hearing Impaired: (800) 231-5469
Foreign Shareholders: (201) 680-6578
TDD Foreign Shareholders: (201) 680-6610

By Internet:
www.melloninvestor.com

All other inquiries should be addressed to:
Investor Relations Department, Station 2197
Emerson
8000 W. Florissant Ave.
P.O. Box 4100
St. Louis, MO 63136-8506
Telephone: (314) 553-2197

DIVIDEND REINVESTMENT AND STOCK PURCHASE PLAN

The Plan is administered by Mellon Bank, N.A., to individual investors who want a convenient, low-cost way to purchase or sell Emerson Electric Co. common stock (NYSE:EMR). You can participate in the Plan if you are a registered holder of Emerson common stock. If you do not own Emerson common stock, you can make your initial purchase directly through the Plan. The Plan provides you with the opportunity to reinvest dividends and is an alternative to traditional methods of buying, holding, and selling Emerson common stock. The Plan is not sponsored or administered by Emerson. For further information and an authorization form, contact the Registrar and Transfer Agent.

DIRECT DEPOSIT OF DIVIDENDS

Stockholders may elect to have dividends electronically deposited into a checking or savings account at a bank, savings and loan institution, or credit union. For details, contact the Registrar and Transfer Agent.

LOW-COST INVESTMENT PLAN

Investors may also purchase their initial shares of Emerson stock through BetterInvesting's Low-Cost Investment Plan. The Plan is not sponsored or administered by Emerson. For details contact:

BetterInvesting (former NAIC)
711 W. Thirteen Mile Rd.
Madison Heights, MI 48071
Toll-Free Telephone: (877) 275-6242 Ext. 331

ANNUAL MEETING

The annual meeting of stockholders will be held at 10 a.m., Tuesday, February 6, 2007, at the Sheldon Concert Hall, 3648 Washington Boulevard, St. Louis, Missouri, 63108. Notice of the meeting, proxy statement, and proxy were sent to stockholders with this annual report.

10-K REPORT

A copy of the Company's 2006 Annual Report filed with the Securities and Exchange Commission on Form 10-K is available to stockholders without charge. To obtain a copy, please contact the Investor Relations Department. The Company's chief executive officer and chief financial officer have furnished the certifications required with the Form 10-K.

CEO AND CFO CERTIFICATIONS

As required by the New York Stock Exchange ("NYSE") listing rules, the Company timely filed its Annual CEO Certification with the NYSE. The Company also filed the CEO and CFO certifications required by Section 302 of the Sarbanes-Oxley Act as exhibits to its 2006 Annual Report on Form 10-K.

INTERNET ACCESS

Corporate news releases, Forms 10-K, 10-Q, and 8-K, the annual report, and other information about the Company are available through Emerson's Web site on the Internet. It may be accessed as follows: http://www.GoToEmerson.com

DUPLICATE MAILINGS

When stockholders own shares in more than one account or when several stockholders live at the same address, they may receive multiple copies of the annual report. To eliminate multiple copies, write to the Registrar and Transfer Agent.

ENVIRONMENTAL PROGRAMS

Information on Emerson's environmental programs may be obtained by contacting:
Environmental Affairs Department, Station 3800
Emerson
8000 W. Florissant Ave.
P.O. Box 4100
St. Louis, MO 63136-8506

RECONCILIATION OF NON-GAAP FINANCIAL MEASURE

	2006
Net Sales:	
Underlying sales (Non-GAAP)	12.5%
Acquisitions, divestitures, and foreign currency translation	3.8%
Net sales (Reported)	16.3%

SAFE HARBOR STATEMENT

This Annual Report contains various forward-looking statements and includes assumptions concerning Emerson's operations, future results, and prospects. These forward-looking statements are based on current expectations, are subject to risk and uncertainties, and Emerson undertakes no obligation to update any such statement to reflect later developments. In connection with the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995, Emerson provides the following cautionary statement identifying important economic, political, and technological factors, among others, changes of which could cause the actual results or events to differ materially from those set forth in or implied by the forward-looking statements and related assumptions.

Such factors include the following: (i) current and future business environment, including interest rates and capital and consumer spending; (ii) potential volatility of the end markets served; (iii) competitive factors and competitor responses to Emerson initiatives; (iv) development and market introduction of anticipated new products; (v) availability of raw materials and purchased components; (vi) government laws and regulations, including taxes; (vii) outcome of pending and future litigation, including environmental compliance; (viii) stable governments and business conditions in emerging economies; (ix) penetration of emerging economies; (x) favorable environment for acquisitions, domestic and foreign, including regulatory requirements and market values of candidates; (xi) integration of acquisitions; (xii) favorable access to capital markets; and (xiii) execution of cost-reduction efforts.

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