

Financial Review

Emerson achieved another record year in 2000, which represented the Company's 43rd consecutive year of increased earnings and earnings per share, and the 44th consecutive year of increased dividends per share.

Results of Operations

Net Sales

Sales for 2000 were a record \$15.5 billion, an increase of \$1,275 million, or 8.9 percent, from 1999. The strong sales growth was driven by robust demand for network power and connectivity products and services, the continued success of other major growth initiatives, and the contribution of acquisitions. This growth was achieved despite divestitures, and the impact of a stronger U.S. dollar that reduced reported sales by more than 2 percent. Underlying sales grew over 7 percent excluding acquisitions, divestitures and currency exchange. All businesses reported sales increases. U.S. sales increased approximately \$1,094 million, or 13 percent, while international sales increased approximately \$181 million, or 3 percent. Underlying sales growth was led by robust demand in the Electronics and Telecommunications business worldwide, while the Heating, Ventilating and Air Conditioning (HVAC) business achieved a very strong performance internationally. New product sales, from products introduced in the past five years, increased approximately \$614 million, to a record \$5.6 billion, representing 36 percent of sales, a 10 point increase in the past five years. The Company continued to reposition into faster-growth markets, divesting three slower-growth operations with combined sales of approximately \$600 million, and acquiring three strategic businesses. Acquisitions completed throughout 2000 had annualized sales of over \$1 billion.

In 1999, sales were \$14.3 billion, up \$822 million, or 6.1 percent, from 1998. The solid sales increase reflected modest underlying sales growth and the contribution of acquisitions. All businesses reported sales increases. U.S. sales increased approximately \$455 million, or 6 percent, while international sales increased approximately \$368 million, or 7 percent. Underlying sales growth was led by strong growth in both the HVAC business and the Electronics and Telecommunications business. New product sales, from products introduced in the past five years, increased approximately \$570 million, or 13 percent, to \$5.0 billion, representing 35 percent of sales.

International Sales

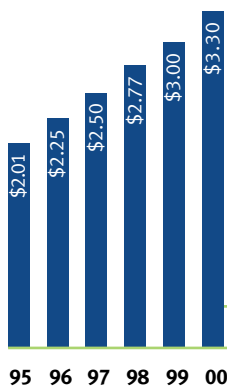
International sales, including U.S. exports, increased over 3 percent to a record \$5.9 billion in 2000, representing 38 percent of the Company's total sales. U.S. exports increased 9 percent to \$1.0 billion. Sales by non-U.S. subsidiaries were \$5.0 billion in 2000, up 3 percent from 1999. International subsidiary sales increased 8 percent excluding acquisitions, divestitures and the unfavorable impact of currency translation of approximately \$320 million. Strong growth in Canada, Asia and Latin America and moderate growth in Europe was dampened by the impact of currency exchange.

In 1999, international sales increased approximately 7 percent to \$5.7 billion, representing 40 percent of the Company's total sales. Underlying growth in Europe, Asia and other regions more than offset the impact of weakness in Latin America. Sales by non-U.S. subsidiaries were \$4.8 billion in 1999, up 9 percent from 1998. U.S. exports decreased 1 percent to \$960 million, primarily reflecting weakness in Latin America and Japan. International subsidiary sales increased approximately 2 percent excluding acquisitions and divestitures.

Business Segment Sales – 2000 vs. 1999

The Process Control business achieved a 5 percent sales increase to \$3.0 billion in 2000. This increase was driven by the Daniel Industries, Inc. acquisition and customers embracing PlantWeb technology, partially offset by difficult market conditions, particularly in Asia and Europe, and the impact of currency exchange. Underlying sales for the year decreased slightly but turned positive in the fourth quarter, the first organic sales improvement since the process markets began to cycle down in 1998. Project quotation activity has improved for several months, which provides confidence that the recent market improvement can continue. Sales of the Industrial Automation business were \$3.4 billion in 2000, up 4 percent, negatively impacted by the stronger U.S. dollar. Solid underlying improvement in Europe and other

Earnings Per Share



Diluted earnings per share increased 10 percent, representing the Company's 43rd consecutive year of increased earnings per share.

international regions, the late-1999 acquisitions of Kato and MagneTek's alternator operations, and stabilization in U.S. capital goods markets drove the improvement. These results exclude the impact of the F.G. Wilson and Krautkramer divestitures.

The Electronics and Telecommunications business achieved outstanding performance, with sales increasing 65 percent, to \$3.3 billion. The increase was the result of underlying growth of nearly 30 percent, reflecting strong worldwide demand for reliable power and networking products, and two strategic acquisitions in 2000 - Jordan Telecommunication Products, Inc. and Ericsson Energy Systems. All product and service areas increased sharply, with particular strength in large UPS and precision air conditioning systems for web-hosting centers, and DC/DC embedded modules for applications such as next-generation routers and telecom switching. Entering fiscal 2001, these operations will represent the Company's largest segment.

Sales of the HVAC business were \$2.5 billion in 2000, a 5 percent increase from 1999, dampened slightly by unfavorable currency exchange. Europe, Asia and Latin America all achieved very strong underlying sales growth, primarily due to improved market conditions and continued penetration of Copeland's scroll compressor technology. The Appliance and Tools business sales rose 7 percent to \$3.4 billion, driven by very strong underlying growth in the tools operations. These results exclude the impact of the Vermont American divestiture. Tools sales through the rapidly growing home centers channel increased in 2000, particularly the successful relationship with The Home Depot, which capitalizes on the RIDGID-branded line of professional quality tools. Underlying appliance-related sales were relatively flat for the year, due in part to distribution issues faced by some key customers.

Business Segment Sales – 1999 vs. 1998

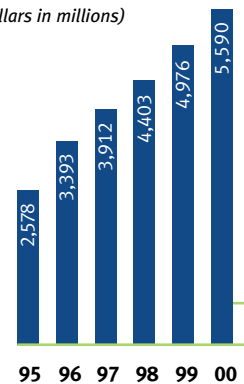
The Process Control business increased sales 7 percent to \$2.9 billion in 1999. This solid sales increase was driven by the strong growth of the PlantWeb initiative, and the Westinghouse Process Control and Daniel Industries acquisitions. Underlying sales decreased, reflecting the impact of weak oil prices on U.S. and Asian demand for process-related equipment, which more than offset modest growth in Europe. Sales of the Industrial Automation business were \$3.3 billion in 1999. Despite widespread softness in end markets, the Industrial Automation business realized a small increase in sales due to the contribution of acquisitions. The global weakness in capital spending, largely due to weak oil pricing earlier in 1999, has had a substantial impact on this business. These results exclude the impact of the F.G. Wilson and Krautkramer divestitures.

The Electronics and Telecommunications business increased sales 35 percent to \$2.0 billion in 1999. This outstanding performance, particularly in the United States and Europe, was achieved due to rapid growth in power protection and environmental equipment, as well as in the service business that monitors and maintains this equipment. This business also benefited from a significant recovery in the market for power supply products, driven by recovery in Asia and robust growth in the computing and telecommunications infrastructure. The increase in the Electronics and Telecommunications business sales was also aided by the 1998 acquisitions of Nortel's Advanced Power Systems operations and Hiross environmental systems in Europe.

Sales of the HVAC business were \$2.4 billion in 1999, an increase of 11 percent from 1998. Underlying sales of the HVAC business increased substantially, driven by a dramatic recovery in residential and light commercial construction in China, a warm summer in the United States, and continued market adoption of scroll technology. Sales of the Appliance and Tools business were \$3.1 billion in 1999, compared with \$3.0 billion in 1998. Underlying sales of the Appliance and Tools business grew slightly, with the results varying by geography and product area. In the United States, strong construction activity drove growth in several consumer-related areas, while European sales declined due to weakness in appliance products. These results exclude the impact of the Vermont American divestiture. During 1999, this business also made substantial gains in home centers, such as The Home Depot and Lowe's, which are experiencing dramatic growth. Also in 1999, the Company contributed its Louisville Ladder operations into a joint venture with Group Imsa SA of Mexico and obtained an equity interest in the venture.

New Product Sales

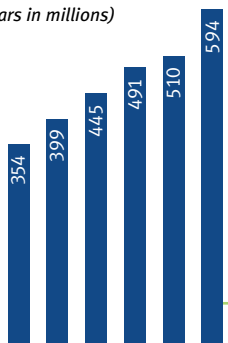
(Dollars in millions)



Sales of new products increased 12 percent in 2000 and represented 36 percent of sales.

Engineering & Development Investment

(Dollars in millions)



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Emerson's commitment to technology is reflected in its increasing investment in engineering and development.

Total Costs and Expenses

Cost of sales for 2000 was \$10.0 billion, an increase of 8.9 percent, due primarily to increased sales volume. In 1999, cost of sales was \$9.2 billion, compared with \$8.6 billion in 1998, an increase of 7.0 percent. Cost of sales as a percent of net sales was 64.4 percent in 2000 and 1999, and 63.9 percent in 1998. Gross profit margins have remained at high levels as a result of the Company's ongoing commitment to cost reduction and containment efforts and productivity improvement programs, offset by the effect of recent acquisitions.

Selling, general and administrative (SG&A) expenses were \$3.0 billion, \$2.8 billion and \$2.7 billion in 2000, 1999 and 1998, respectively. As a percent of net sales, SG&A expenses were 19.2 percent, 19.4 percent and 19.9 percent in 2000, 1999 and 1998, respectively. The decrease in SG&A as a percent of net sales was primarily the result of volume leverage on sales growth, partially offset by new product development and other revenue growth programs. The Company continued its commitment to technology investment by increasing engineering and development expense 16 percent to a record \$594 million in 2000, compared with \$510 million in 1999 and \$491 million in 1998.

Interest expense increased to \$288 million in 2000 from \$190 million in 1999, primarily reflecting an increase in average borrowings due to acquisitions and higher interest rates. In 1999, interest expense increased from \$152 million in 1998, reflecting higher average borrowings resulting from acquisitions and share repurchases.

Other deductions, net, including amortization of intangibles, were \$75 million in 2000, compared with \$95 million and \$100 million in 1999 and 1998, respectively. Fiscal 2000 included a gain of \$80 million from the disposition of the Company's interest in the Krautkramer non-destructive testing business and a gain of approximately \$37 million due to the disposition of the Company's interest in Vermont American. Fiscal 1999 included a gain of \$64 million from the disposition of the Company's interest in F.G. Wilson. These gains were substantially offset by other non-recurring items. See note 3 for additional information.

Income Before Income Taxes

Income before income taxes increased \$157 million, or 7.8 percent, to \$2.2 billion in 2000, reflecting a strong sales increase, programs to generate improvement in underlying margins and the negative impact of currency translation. Earnings before interest and income taxes in the Process Control business were \$274 million in 2000, a decrease from 1999, reflecting weak demand in the process markets and a stronger U.S. dollar. The Industrial Automation business earnings increased \$27 million to \$465 million in 2000, due to moderate sales growth and acquisitions, partially offset by currency exchange. Earnings of the Electronics and Telecommunications business increased \$221 million, or 95 percent, to \$454 million in 2000, due to robust sales growth and acquisitions. Earnings of the HVAC business increased \$21 million, or 6 percent, to \$382 million in 2000, driven by very strong sales growth in international markets. The Appliance and Tools business earnings increased to \$562 million, or \$17 million, in 2000, reflecting increased sales volumes in the tools operations. See note 12 for additional information by business segment and geographic area.

Income before income taxes increased \$97 million, or 5.1 percent, to \$2.0 billion in 1999, reflecting increased sales and improvement in underlying margins, partially offset by increased interest expense. The base company (excluding acquisitions and divestitures) realized an outstanding performance in 1999, increasing underlying operating margins approximately 0.5 points. This improvement was offset by the acquisition of businesses with lower margins. Earnings before interest and income taxes in the Process Control business were \$313 million in 1999, a decrease from 1998, reflecting weak demand associated with lower oil prices and higher expenditures for cost reduction efforts and productivity improvement programs. The Industrial Automation business earnings increased \$18 million to \$438 million in 1999, driven by cost containment measures that mitigated the impact of a challenging economic environment. Earnings of the Electronics and Telecommunications business increased \$92 million, or 65 percent, to \$233 million in 1999, due to strong sales growth and the acquisition of the Advanced Power Systems

business. Earnings of the HVAC business increased \$45 million, or 14 percent, to \$361 million in 1999, reflecting strong sales growth in both U.S. and international markets. The Appliance and Tools business earnings increased \$24 million to \$545 million in 1999, reflecting varying results by geography and product area.

Income Taxes

Income taxes were \$756 million, \$707 million and \$695 million in 2000, 1999 and 1998, respectively. The effective income tax rate was 34.7 percent in 2000, compared with 35.0 percent in 1999 and 36.1 percent in 1998, reflecting ongoing global tax planning strategies and the impact of acquisitions and divestitures.

Net Earnings and Return on Equity

Net earnings for 2000 were a record \$1.4 billion, up 8.3 percent from \$1.3 billion in 1999. Net earnings as a percent of sales was 9.2 percent in 2000 and 1999. Diluted earnings per common share were a record \$3.30 in 2000, up 10.0 percent from \$3.00 in 1999. Earnings per share excluding goodwill amortization, a metric that management believes is more indicative of cash operating performance, were \$3.63 in 2000, up 11.0 percent from \$3.27 in the prior year. Emerson achieved a return on average stockholders' equity of 22.6 percent in 2000 and 21.9 percent in 1999 and 1998. Net earnings for 1999 were up 6.9 percent from \$1.2 billion in 1998. Diluted earnings per common share in 1999 were up 8.3 percent from \$2.77 in 1998. Earnings per share excluding goodwill amortization in 1999 were up 9.4 percent from \$2.99 in the prior year.

Financial Position, Capital Resources and Liquidity

The Company continues to generate substantial cash from operations and remains in a strong financial position with resources available for reinvestment in existing businesses, strategic acquisitions and managing the capital structure on a short- and long-term basis.

Cash Flow

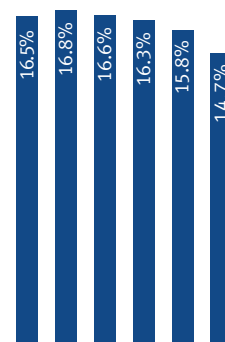
Emerson generated operating cash flow of \$1.8 billion in 2000, up 1.6 percent from the prior year. Operating cash flow in 1999 increased 9.6 percent compared with \$1.7 billion in 1998. Success with lean manufacturing efforts to decrease inventory and a program to improve the receivable collection cycle resulted in a reduction of average operating working capital as a percentage of sales, a measure of working capital efficiency. In 2000, this measure improved to 14.7 percent compared with 15.8 percent and 16.3 percent in 1999 and 1998, respectively.

The growth in cash flow was negatively impacted by divestitures, taxes paid on the related gains, and the inclusion of fast-growing acquisitions and associated working capital not included in the prior year. Underlying cash flow improved 7 percent in 2000 and can be analyzed as follows (dollars in millions):

	<u>2000</u>	<u>1999</u>	<u>Change</u>
Underlying cash flow	\$ 1,884.6	1,755.8	7.3 %
Acquisitions/Divestitures	(44.8)	54.7	
Total cash flow	\$ 1,839.8	1,810.5	1.6 %

Capital expenditures were \$692 million, \$592 million and \$603 million in 2000, 1999 and 1998, respectively. These expenditures increase the Company's global capacity to leverage opportunities within the heating, ventilating and air conditioning and network power and connectivity markets, as well as improve manufacturing productivity in a number of businesses. Cash paid in connection with Emerson's purchase acquisitions was \$1,972 million, \$1,202 million and \$573 million in 2000, 1999 and 1998, respectively.

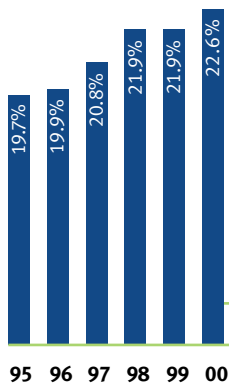
Operating Working Capital as a Percent of Sales



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Average operating working capital has improved from 17 percent of sales in 1995 to 15 percent in 2000.

Return on Equity



Return on equity increased to 22.6 percent in 2000.

Dividends were a record \$613 million (\$1.43 per share, up 10 percent) in 2000, compared with \$566 million (\$1.30 per share) in 1999 and \$521 million (\$1.18 per share) in 1998. In November 2000, the Board of Directors voted to increase the quarterly cash dividend 7 percent to an annualized rate of \$1.53 per share. Success with repositioning and internal initiatives to increase underlying growth has created significant new investment opportunities, and over time, the Company intends to moderate the dividend payout ratio toward a range of 40-45 percent of prior year earnings, providing greater flexibility to pursue these opportunities. The cash dividend will continue to be supplemented with the share repurchase program. The repurchase program, initiated in fiscal 1997, authorizes the repurchase of up to 40 million shares of the Company's outstanding common stock, with nearly 30 million shares repurchased through September 30, 2000. The pace of repurchase has slowed with repositioning, and this program is anticipated to extend into 2002 or 2003. Net purchases of treasury stock totaled \$376 million and \$324 million in 2000 and 1999, respectively.

Leverage/Capitalization

Total debt increased to \$4.6 billion in 2000, from \$3.3 billion in 1999 and \$2.6 billion in 1998, reflecting the impact of acquisitions and the Company's share repurchase program. The total debt-to-capital ratio was 41.8 percent at year-end 2000, compared with 34.6 percent in 1999 and 30.8 percent in 1998. At September 30, 2000, net debt (total debt less cash and equivalents and short-term investments) was 40.2 percent of net capital, compared with 32.7 percent in 1999 and 29.0 percent in 1998. The Company's interest coverage ratio (income before income taxes and interest expense divided by interest expense) was 8.6 times in 2000, compared with 11.7 times in 1999 and 13.7 times in 1998, as a result of higher average borrowings and interest rates in 2000, partially offset by increased earnings. See notes 3, 4 and 5 for additional information.

At year-end 2000, the Company and its subsidiaries maintained lines of credit amounting to \$3 billion to support commercial paper and had available non-U.S. bank credit facilities of \$560 million to support non-U.S. operations. Lines of credit totaling \$1.5 billion are effective until 2005, with the remainder through June 2001. These lines of credit and bank credit facilities assure the availability of funds at prevailing interest rates. In addition, as of September 30, 2000, the Company could issue up to \$500 million of additional debt securities under its shelf registration with the Securities and Exchange Commission.

Financial Instruments

The Company is exposed to market risk related to changes in interest rates 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 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. See notes 1, 4, 5 and 6.

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities." The statement, as amended, requires the recognition of all derivatives at fair value in the balance sheet and establishes new hedge accounting rules. The adoption of the statement in 2001 is not expected to have a material effect on the Company's operating results or financial condition.