Q4 2007 Earnings Conference Call

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Good morning, I'm Matt Ginter, head of investor relations for 3M, and I would like to welcome all investors and analysts to our fourth quarter 2007 business review.

You will find this morning's presentation on our investor relations website at 3M.com. These slides will remain on the site, along with an audio replay of today's call, for an extended period of time.

If you would, please take a moment to read the forward looking statements on slide 2. During today's conference call, we will make certain predictive statements that reflect our current views and estimates about our future performance and financial results.

These statements are based on certain assumptions and expectations of future events that are subject to risks and uncertainties.

Item 1A of our most recent forms 10K and 10Q lists some of the most important risk factors that could cause actual results to differ from our predictions.

George Buckley, our CEO, and Pat Campbell, our CFO, will both make some formal comments today, and then we will get to your questions.

We know how busy you all are during the earnings season, so we will do everything in our power to keep today's call at about one hour. You can help us during the Q&A by limiting yourself to one question and one follow-up, so that all questions can be properly addressed.

So now please go to slide number three, and I'd like to turn the program over to Pat Campbell. Pat…..

Patrick D. Campbell – Senior Vice President and CFO

Thanks Matt and good morning everyone and thank you for joining us today.

We manage our company to drive sustainable long-term shareholder value. And while it is certainly critical that we regularly assess our interim quarterly progress against our objectives, it is equally if not more important that we examine our results over the longer term. So today I will begin with a summary of a few critical full-year metrics before I get into the fourth quarter results.

By all accounts 2007 was a very good year for 3M. The numbers I will quote on this slide exclude the impact of divested businesses, primarily pharmaceuticals, and special items in all periods.

Sales were up 10.5 percent for the year with a record 63 percent of our sales coming from our international operations, which is a testament to the strength of our unparalleled international capabilities.

Earnings per share rose nearly 17 percent, driven primarily by a 12% operating profit improvement. Operating margins stayed flat year-on-year at 22.5%.

Capital efficiency is another critical measurement for us, and we strive to balance investments to accelerate growth with the necessary operating discipline in order to sustain 20 percent-plus ROIC. In 2007, return on invested capital was 21.4 percent, about equal to last year, again excluding the impact of divested businesses.

Finally, we returned over $4.6 billion dollars to shareholders in 2007 via a combination of dividends and share repurchases. This was an all-time annual record and a hefty 24% increase over the prior year.

So all in all, 2007 was a very successful year for 3M. We continued to execute our investment strategy to accelerate future growth while maintaining premium returns and double-digit earnings growth. And at the same time we rewarded our shareholders handsomely. As with any long-term strategy, there is still much to be done, most notably in accelerating our sustainable top-line growth rate, but our plan remains on track and I am very pleased with our progress to date.

Please go to slide number 4, and let's turn our attention to the fourth quarter.

This was another very good quarter for 3M, with healthy sales and profit increases despite some continued tough end-markets in the United States. We managed to post another record sales quarter at $6.2 billion dollars, an increase of 11 percent adjusted for divested businesses and helped by a favorable currency impact of 4.7 percent. The rest of the discussion of this slide excludes the impact of divested businesses.

One of 3M's indelible strengths is the breadth of its portfolio, and the fourth quarter was another shining example of this. In dollar terms, all six of our businesses grew sales year-on-year, led by Health Care at a whopping 22.4 percent, and we also saw strong double-digit growth in both Industrial and Transportation and in Safety, Security and Protection Services. And on a local-currency basis, five of those same six businesses posted positive growth. So there is no doubt that our portfolio is stronger today than it was just a short while ago, as more businesses are contributing to growth each and every day. This certainly gives me confidence looking into the future.

Looking at the company geographically, we again drove broad-based growth, with double-digit dollar sales growth in Europe, Latin America and Canada, excluding divestitures. Even after excluding positive currency impacts, local currency growth was positive in every major region of the world.

Fourth quarter earnings were $1.19 per share. This figure excludes approximately 2 cents of cost related to restructuring actions due to the forming of a new Projection Systems organization and selective reductions to better balance the structure in a few of our businesses that are experiencing slower end markets, mainly in the U.S., that primarily impacted our Display and Graphics and Industrial and Transportation businesses. While certainly not everything went right in the quarter and we can always perform better, we did manage to increase sales and EPS by 7 and 8 percent respectively excluding special items, or 11 and 14 percent further excluding divestitures, which I am very pleased with in this tough economic environment.

Now let's dig a little deeper into the quarter. Please turn to slide number 5. All information on this slide excludes special items.

Fourth quarter gross margins were 46.9 percent and operating margins were 20.8 percent. Both were in line with last year's fourth quarter, after adjusting for the impact of divestitures.

SG&A expense was up 5.7 percent year-on-year to $1.3 billion, or up 11.7 percent adjusted for divestitures. This increase is somewhat higher than is typical for us, but remember that a weak dollar inflates our costs just as it does our sales. So the 11.7 percent increase, when compared with our 11 percent sales increase ex-pharma is much more reasonable.

So let's break down SG&A a little further. Administrative costs, adjusted for the pharma divestiture and for currency, were about flat year-on-year, so we continue to leverage G&A.

Selling expenses, which include sales reps, marketing, advertising and the like, were up 9 percent excluding divestitures and currency impacts. We invested most heavily in two businesses, one of which was Health Care in areas such as oral care, medical and through recent acquisitions such as Biotrace, Accolyte and Softmed, where we are investing today for growth tomorrow. And in Consumer and Office, we have stepped up our investment in brands to support the long-term health of this business and to drive sales with our customers.

Research and development and related expenditures were up nearly 13 percent year-over-year, excluding divestitures, driven by Health Care and Industrial and Transportation to support our underlying strategy to reinvigorate our core business.

Operating income was $1.3 billion, an increase of 5.2 percent, or 11.2 percent, excluding divestitures.

Non-operating expense was $33 million, up $11 million year-on-year. $8 million of this increase was due to an impaired auction-rate security that we wrote off during the quarter.

The fourth quarter tax rate was 30.7 percent, up slightly from last year's 30.3 percent rate.

And finally, earnings per share were $1.19, a year-on-year increase of 8.2 percent. Again, adjusting for divestitures, mainly the pharmaceuticals business, EPS increased 14.4 percent.

Next, let's peel the onion back a little further by looking at the components of our fourth quarter sales improvement. Please turn to slide 6.

In US-dollar terms, global sales increased 7.3 percent, or 11 percent adjusting for divestitures, primarily the pharma business. International sales growth ex-divestitures was 13.5 percent, while the US operations expanded sales by 6.7 percent.

Of course we continue to benefit from favorable currency comps, primarily the stronger Euro. Currency impacts added 4.7% to worldwide sales growth so, on an ex-currency basis, total local currency growth was 6.3 percent globally.

In the United States, total growth was 6.7 percent, led by strong performance in three of our segments: Health Care, Industrial and Transportation and Electro and Communications businesses. Sales were down slightly in our other three business segments due to a slow down in a handful of divisions tied to residential construction, consumer spending, highway construction and consumer electronic devices that have come to end of life. Acquisitions in Industrial and Transportation and Health Care accounted for most of the 3.8 percent acquisition growth in the US, organic volume added 1.9 percent and selling price changes added a full percent to growth in the quarter.

International total local currency growth in the fourth quarter was 6.1 percent. Latin America led the way with 16.2 percent growth as 5 of 6 businesses within that region posted strong double-digit growth rates. Europe grew by 6.4 percent, led by Health Care at 18.4 percent. Rounding out international, Asia Pacific and Canada both drove total local currency growth of approximately 4 percent. The Asia Pacific region had their strongest quarterly local currency growth of this year. Organic volumes increased 5 percent in international with double digit volume growth from emerging markets of 10.3 percent, acquisitions added 1.3 percent, and selling prices were down just slightly in the fourth quarter.

Let me turn to our business segment results now. This discussion excludes special items in all periods. Please turn to slide 7 for a summary of results for our largest segment—the Industrial & Transportation business.

Industrial and Transportation had another strong quarter, with sales up 13.7 percent to $1.9 billion. Local currency sales increased 7.8 percent, including 4 percent from acquisitions. Operating income increased 13.5% to $360 million with margins right in-line with last year at 19.1%. Full year sales increased 9.6 percent to $7.3 billion while profits increased 11.3 percent to $1.5 billion. The Industrial and Transportation team's strong operational discipline drove an all-time record full year operating margin of 20.8 percent, up 40 basis points versus last year. Over the past 4 years this business has improved operating margins by nearly 500 basis points.

The contributions to sales growth in the fourth quarter were similar to previous quarters as the largest divisions within Industrial and Transportation continue leading the way; most notably, Industrial Adhesives and Tapes, Abrasives, Automotive Aftermarket and Automotive OEM divisions. Energy and Advanced Materials division showed strong performance due to strong market focused programs in the oil and gas industry and solar industry. 3M's proprietary glass bubble material is widely used in weight reduction applications such as construction of deep oil wells, aerospace and automotive industries.

Internationally, full year sales growth was strong across the regions. Significant manufacturing investment was made in emerging economies such as India, China and Poland to simplify supply chain and get closer to local customers. As a result Industrial and Transportation Business continues to generate over 20% of its growth in emerging economies resulting in roughly $1.2 billion dollars of business coming from emerging economies.

The increased focus and technical investment in our core Adhesives, Abrasives and Tapes platforms continues to drive growth in this segment across the many markets we serve, notably industrial, automotive, aerospace, energy, and filtration, just to name a few. 3M is clearly recognized as the number one brand of choice in adhesives and tapes categories globally.

In addition, during the fourth quarter the Industrial and Transportation business added four more gap filling acquisitions, bringing the total to seven for the year. In combination with our focused investments in R&D, these acquisitions will help to strengthen our core tapes, adhesives and abrasives platforms for many years to come.

Please turn to slide 8, where we will discuss the fourth quarter and 2007 highlights for our Health Care business.

Health Care completed an outstanding 2007 with a very strong fourth quarter. Excluding pharma, quarterly sales rose more than 22 percent year-on-year. Local currency sales were up 17 percent versus last year, driven primarily by organic growth but also boosted 3.5 points by acquisitions. Much of the acquisition growth came from two deals that closed in late 2006—Biotrace International, PLC, a UK-based provider of microbiology products, and SoftMed, a Maryland-based provider of health information software solutions. In total, Health Care added 5 acquisitions in 2007 to strengthen the portfolio and accelerate growth into the future.

Also included in this quarter's result was 3.7 points of growth due to supply agreements related to the sale of our branded pharmaceuticals business, in which our Drug Delivery Systems Division became a supplier to the acquiring companies.

Excluding pharma, fourth-quarter profits were up 18.7 percent, to $286 million.

Health Care's full-year results were equally impressive. Sales rose nearly 23 percent and operating income surged 19 percent, both excluding the impact of pharma. Full-year local currency sales growth was 18.3 percent, largely organic, and including 4.5 percent from the pharma supply agreements. Acquisitions added 4.4 points to full-year growth in Health Care.

The Health Care portfolio really hit on all cylinders in 2007, as every division posted double-digit sales growth for both the fourth quarter and the year led by medical supplies, Drug Delivery and Health Information Systems. Our portfolio of market-leading products in Medical includes infection prevention solutions, skin and wound care therapy including surgical preps and drapes, Tegaderm brand transparent dressings, medical tapes, Littmann brand stethoscopes and cardiac monitoring electrodes. In Drug Delivery Systems, we drove strong growth in HFA-based components for drug inhalers. HFA is an environmentally friendly propellant, pioneered by 3M, that is superior to traditional ozone-depleting CFC's. We also saw strong growth in Health Information Systems, where 3M is the worldwide expert in healthcare funding and performance management solutions for the hospital market.

In oral care, we continue to drive core growth in the areas of dental restoratives and cavity prevention along with aesthetic products in both the dental and orthodontic channels.

Looking geographically, Health Care, ex. pharma, achieved double-digit sales growth rates in all major regions.

Please turn to slide 9 for a review of the fourth quarter and full year results for our Display and Graphics segment.

Display and Graphics sales were just shy of $1 billion dollars in the fourth quarter, up slightly year-over-year, and profits were a hefty $252 million although down a few points year-on-year.

Sales growth was negatively impacted by nearly one percent due to the third-quarter divestiture of our Opticom and Canoga loop businesses, both of which were good businesses but no longer considered strategic to our portfolio.

Fourth-quarter local currency declined slightly in Display and Graphics. On the positive side, Commercial Graphics division posted another solid quarter to finish the year on a positive note. Throughout 2007 we saw strong performance in the vehicle wrapping market where we provide films, inks and other products for this "rolling billboard" industry. Full-year sales grew solid single digits on a local-currency basis in this, one of our largest divisions.

In Traffic Safety Systems, which is also one of our largest divisions, local currency sales were down slightly in the fourth quarter and grew at a low-single-digit clip for the full year. Not surprisingly, we grew faster outside the United States throughout 2007 as our market-leading reflective solutions for highway construction projects are a perfect match in developing economies that are adding infrastructure. In the United States, the road construction market continues to be burdened by significant inflation on road surface materials such as asphalt and concrete, which diverts spending from other construction products such as our reflective sign sheeting.

Both Commercial Graphics and Traffic Safety Solutions are absolutely fabulous 3M franchises that often get overlooked. Both command leading market positions, are highly profitable and they set the pace for innovation, quality and service in their respective markets.

Offsetting this growth was a low single digit decline in our Optical Film business.

Profit margins for the quarter were 26.4 percent, or down 1.1 percentage points year-on-year, driven by our optical film business which we anticipated and described at our December investor meeting in New York.

We remain keenly focused on market segmentation in this business, with strong penetration in handhelds, computer displays and LCD televisions. We continue to face attachment rate pressure in the computer monitor and LCD TV segments although in the fourth quarter we did see a mix-shift back to 1080p TVs. This is good for our business as 3M optical films are used more heavily in 1080p sets. We believe over the longer term that 1080p LCD TV's will gain an increasing share of the overall LCD TV market.

We remain optimistic about the longer-term prospects for our optical film business, though we will face continuing price down and attachment rate pressure in 2008 as we adjust our prices to meet our customer's needs. Our continued investment in this business has led to a solid stream of new products that our customers are very excited about and will allow us to maintain our market leadership in brightness enhancement. Our films also offer a unique environmental solution through reduced energy consumption – an increasingly important requirement from both retail customers and government agencies.

Full-year sales in Display and Graphics grew 3.2 percent, and profits rose 3.7 percent to $1.1 billion. Operating margins were 29 percent for the year, up 20 basis points over 2006

Please now turn to slide 10, for details on our Consumer and Office business. Based on the business conditions of the U.S. customers this business turned in very good results.

Sales in this segment increased 6.6 percent to $859 million in the fourth quarter with local currency sales up 2.6 percent. While this is below our longer-term run-rate in this business, it is truly an outstanding result considering the difficult sales environment for the U.S. retail and office markets. Unlike most of our business portfolio, the business has 60 percent of global sales in Consumer and Office in the United States.

Fourth-quarter worldwide sales growth was led by our construction and home improvement business, where we are driving penetration in the DIY retail channel with market-leading products such as Scotch Blue Painters tape, Filtrete home furnace filters, and Command mounting and fastening products, just to name a few. We also drove good growth in the home cleaning category with our family of scouring and cleaning products. And finally, we saw a nice rebound in the office supplies area with low-single-digit local-currency growth in the quarter.

Looking across geographies, our international operations had an outstanding fourth quarter. Sales in dollars grew at double-digit rates in Europe, Asia Pacific and Latin America as we are committed to expanding our international penetration.

Operating profit was up slightly in the fourth quarter to $155 million, and margins were a solid 18.1 percent.

For the full year, Consumer and Office sales grew at a healthy 7.6 percent clip and operating profits rose 9.3 percent. Operating margins increased 30 basis points year-on-year, exceeding 20 percent.

Please turn to slide 11 for a review of our Safety, Security and Protection Services segment.

Sales in this business grew 11.3 percent in the fourth quarter, led by our in respiratory protection, corrosion protection and building and commercial service businesses. Local currency growth was 5.3 percent including 2.4 percent from acquisitions, primarily E. Wood, a U.K.- based provider of corrosion protection products. For the first time this year we saw year-on-year growth, albeit small, in our roofing granules business, which supplies mineral used on asphalt shingles for the residential housing market. While this is a positive result it is still too early to know if this business is turning a corner as the U.S. housing market continues to remain weak going into 2008.

Geographically, we drove strong double-digit growth in the quarter led by Europe and, to a lesser extent, Asia Pacific and Latin America.

Fourth-quarter operating income rose 10.3 percent to $133 million and margins were almost 18 percent.

For the full year, sales increased 15.3 percent with local currency sales of 10.8 percent. Acquisitions contributed 7.4 percentage points to local currency growth, primarily Security Printing Systems Ltd and E Wood.

Full-year sales growth was led by our respiratory protection business, followed by security systems, corrosion protection and building and commercial services. 2007 growth was held back by market softness in the U.S. residential construction market, which negatively impacted our roofing granules business. This softness reduced full year growth in Safety, Security and Protection Services by about 1.5 percent.

Worldwide operating income for 2007 was $640 million, up almost 15 percent versus 2006. and full-year margins were a robust 21 percent.

Finally, during the year we added a couple of small but strategic gap fill acquisitions in E. Wood and Rochford Thompson. We also announced a more sizable acquisition on November 15th, Aearo Technologies, a global leader in the personal protection industry. Aearo will significantly broaden our safety solutions beyond our existing industry-leading respiratory protection products line-up. We continue to expect the Aearo acquisition to close towards the end of the first quarter of 2008.

Please turn to slide 12.

Electro and Communications sales grew 7.3 percent in the fourth quarter. Local currency growth was 2.4 percent, about one-half of which was acquisition-related. Growth in the quarter continued to be led by our electrical markets business, a leading provider of insulating, protecting and sensing solutions for the electrical trades and power producers, along with the electronics markets materials business that serves the consumer electronics industry with high-value specialty tapes, adhesives and fluids. Fourth-quarter operating profit increased almost 17 percent to $120 million.

Our flexible circuits business, which supplies components primarily to the ink jet printer market, continues to weigh on overall segment results as the ink jet market becomes commoditized and a number of applications go end-of-life. Softness in this business held back overall Electro and Communications sales and profit growth by 3 percent and 13 percent, respectively in the quarter.

For 2007 in total, Electro and Communications had a truly outstanding year, especially considering that flex circuits hurt total segment sales and profit growth by 2.5 percent and 9.3 percent, respectively. Total sales growth was 5.5 percent, with 2.3 percent local-currency growth including a point-and-a-half boost from acquisitions. Growth was led by the Communications and Electrical Markets divisions as they both excelled in delivering double digit percent increases in sales and profits in 2007.

Geographically, growth was consistent across all regions, led by Europe and the U.S.

The Electro team has done a remarkable job over the years driving productivity and taking aggressive actions to improve its competitiveness, and 2007 was no exception. Full-year profits increased 14.2 percent and margins were almost 19 percent.

Please turn to slide 13, where I will review a few balance sheet and cash flow metrics.

Free cash flow in the fourth quarter was just shy of $1.3 billion versus $900 million in last year's fourth quarter, adjusted for timing differences related to pharma divestiture gains. And while you don't see it on this chart, full-year free cash flow was $3.5 billion, up over 30 percent versus last year's $2.7 billion figure.

Income tax timing differences can sometimes swing our free cash flow in any given period, as was the case in both 2006 and 2007.

Working capital turns improved sequentially by 0.3 turns, and were about in-line with same quarter last year.

Capital expenditures in the fourth quarter totaled $391 million, not too dissimilar from both year-on-year and sequentially. For 2007 we invested a little over $1.4 billion in capital expenditures, which was near the low-end of our full year expected range of $1.4 to $1.5 billion.

Dividend payments to our shareholders were $341 million, and we continued to buy back stock during the quarter with gross share repurchases of $483 million. For the total year we returned $4.6 billion of cash to our shareholders via a combination of dividends and share repurchases, which is the most of any year in our history. Weighted average diluted shares outstanding were down 3.1 percent year-on-year, and down slightly on a sequential basis.

And finally, our debt to capital ratio was 30 percent at the end of the year.

This concludes my formal business review. Now I would like to hand the call over to George for a recap of 2007 and our outlook for 2008.

George W. Buckley – Chairman, President and CEO

Thank you very much Pat, well done, and a sincere welcome to all of our listeners this morning. I'll make a few brief comments about the quarter and year, our 2008 outlook, and then we'll be happy to address your questions.

Needless to say, this was a very good quarter for 3M with operating earnings a couple of pennies above consolidated expectations, excluding a couple pennies also of special items that we had in the quarter. Pat has already outlined the growth numbers, but just for emphasis, we achieved over 7% sales growth and 11% in the quarter after correcting for Pharma which I think is pretty good in this environment.

Obviously we are pleased with the good Q4 performance, but the real issue here is not what we did in the fourth quarter but our outlook for 2008, and, importantly, how that outlook may or not impact our longer-term strategic plan.

I can imagine a question you are asking yourself right now is "how immune or otherwise is a company like 3M to slowing economic trends?" So before going into 2008 guidance, I want to outline to you how 3M's sales might be affected by our presence in various kinds of markets.

We've been asked by investors if we lead, follow or are concurrent with market trends. Essentially, the question is, are the current earnings trends an indicator of what is to come, ... what is here now, ... or what is past?

Before beginning to answer that question, I want to stress again that 63% of 3M's sales were outside the United States in 2007 and this will increase to about 65% in 2008. When you look at it this way, 3M is in fact a broad based international company that seems to be masquerading as a US company.

I'd like also to get an accurate set of sales numbers by geographic region out on the table. In 2007, sales in Latin America were 7% of the total, in APAC they were 27%, in Europe, Middle East and Africa 26%, in Canada 3% and in the US they were 37%. In 2008, the US will be about 35% of total sales.

It is important to note also that $7 billion of our global sales, or nearly 30 percent of the total, are generated in emerging economies such as central and east Europe, developing Asia and Latin America. These sales have been growing almost 20 percent annually over the past five years. Allow me to stress please that there is no company that I know of, even ones much larger than us, that can match 3M's capabilities with respect to international distribution.

I'd like to spend a few minutes discussing our four principal channels of distribution and their relationship to economic trends. These are: first, the mass retail market channel; second, industrial distribution; third, our OEM channel and fourth, Health Care.

In our Consumer and Office business, our method of distribution is mostly through mass channel retailers. To get the size of this business in perspective, in 2007, 58% of the total sales of this segment were US based, equal to 8% of total 3M sales. This consumer channel is the one which is closest to day-to-day economic cycles in the US. Living in that space can feel like you are taking the pulse of the economy on a real-time basis every day and that is how sales vary. We make Post-it notes today, ship them to a retailer tomorrow and they are sold to a consumer on Monday.

Industrial distribution is a channel which, because it is a bit farther back up the supply chain, lags the economy a little, perhaps by a month or so. This channel amounts to 30% of 3M sales. We supply hundreds of large and thousands of small distributors around the world via this channel.

The third channel on my list, OEM channel is one where the parts we make are "spec'd" into another product. We service such industries as telecom (via infrastructure build-out, upgrade and refurbishment), electronics (through TVs, handheld devices, phones or test and measurement equipment) and the automotive industry, among others. We also service the oil and gas, mining and aerospace industries through this channel as well as through general distribution. Of course these sales, while locked in by specification, follow the cycles of the markets they serve or the success of the products they eventually become part of.

Lastly, we have some large, strong, cycle-resistant businesses. For example, our sizeable Health Care business here in the US, which is $4Bn in total and $1.8Bn in the US which is 20% of total US sales, is largely immune to economic cycles as is the automotive aftermarket. The same can be said about a large part of our safety and security business, which is another $3 billion, which will reach almost $4 billion annualized run rate by the end of 2008.

In addition, we're driving some good growth platforms such as oil and gas, alternative energy, mineral extraction and aerospace. These elements help offset the impact of channels or businesses which may erode a little in economic downturns.

On balance, the sales mix we have means we are somewhere between concurrent with the market or a few weeks of lag. Those parts of our business which are close to the consumer would tend to go into decline first and faster than some of our peers who have long cycle product streams, but they also come out a lot faster. Sales can also be distorted by inventory corrections, both on the way down as well as on the way up, and often at some times in between. So all in all cyclic downturns, when they occur, tend to be much less persistent and pervasive for 3M than other companies with long cycle portfolios… and much more attenuated because of the huge regional and business market diversity we have.

There are many challenges that companies like 3M face. But two of the biggest are to resist temptation… specifically the temptation to add cost when times are good… and to cut R&D or other growth investments when times are more challenging. We were courageous these past two years in taking on a large list of restructuring, reinvestment, rebuilding and reinvention activities as a means of assuring a strong future for 3M.

In 2007 we invested heavily in the future. We exceeded our external growth commitments even as we were investing to reinvent sizeable parts of 3M for the long term. We've made enormous strides in getting our manufacturing footprint right by opening new plants in Korea, three in China, and one each in Russia, India, Canada, Mexico and Turkey, plus several plant extensions in the US. In 2007 we also closed inefficient plants in the US, in Italy, Japan, Canada and New Zealand

and downsized others in the US and UK. We have closed over 50 inefficient plants around the world in the last five years.

In 2007, you'll note that we increased R&D spending ex-divestitures by 11.4 percent yet carried that increase in our earnings numbers. We invested $20 million on plant start-ups and we also invested tens of millions of dollars on a number of emerging business opportunities, again all to accelerate growth momentum. All of these investments were washed into operating earnings.

One of the real benefits of this extra R&D effort is that we now able recycle appreciable amounts, somewhere around 20% and increasing, of waste material on BEF production that was formerly disposed of in Landfills. We are also now able to recycle somewhat smaller percentage amounts on DBEF. The early signs are that our Optical System penetration strategy is beginning to get traction with encouraging signs on volume wins.

We opened up new markets in Kazakhstan and North Africa, investing and spending in the "here and now" to get the later benefit of growth and penetration in these very attractive markets.

On the capital front, we spent hundreds of millions of dollars adding capacity close to our customers and getting our supply chain straightened out. While much was achieved, much remains to be done in this area.

We continued on course with strategic M&A, with 16 acquisitions that built new competencies in product and markets where we needed it. As much as anything here, acquisitions bought us speed in reducing time to market. All these actions are helping us build an incredibly powerful company for the future even as we deliver in the short term.

In 2008 we expect that we will generally continue this investment pattern, and that assumption is baked into our forecast earnings. That said, we will always use prudence and circumstance to guide to the size and timing of our actions. In 2008, we will make appropriate real-time judgments on investments with constant attention to economic circumstances. Our approach to investing in the future is a practical approach, and not blindly ideological.

In 2007 we drove $1.5 billion of growth, or $2.3 billion of growth ex-divestitures. To put this in perspective, this is almost as big as our Electro and Communications business today. All business segments contributed to this growth. And the growth came in many different ways. There was simple penetration with existing products such as Filtrete brand home filters in Consumer and Office segment, which, by the way, is rapidly becoming the next enduring 3M franchise. And there were many new product launches and R&D revitalizations and localizations, such as our acquisitions of dental and medical companies in Brazil, Chile and Thailand or entirely new product or service segments such as passport production in the UK. An awful lot was done here in this company last year.

We made great progress on the costs of the aluminum composite conductor program we've spoken often about, which has the potential to significantly change the way in which electricity is distributed. And anybody who went to the recent CES show in Las Vegas perhaps saw our new micro projector that will fit in the palm of your hand. Several companies have expressed key interest in this product and we are going all-out to commercialize and capitalize on it as soon as possible. Innovation is again alive and well at 3M.

One of 3M's great strengths is that there is no one, single source of growth. We are very diverse, market wise and geography wise and therefore growth patterns are likely to be repeatable and extendable. In my view, this makes us the right kind of investment bet in times like these, and also for the long term.

I would be remiss if I did not continue to stress the long term health of 3M. Within 10 years your life will have changed significantly and 3M will be driving a lot of that change. Your personal life will be impacted most by technology and innovation. Hospitals will be safer because of 3M's infection detection platforms, you will use less energy, in part driven by 3M's products, solar will become a bigger piece of your life, in part due to 3M, your security fears will ease, again because of 3M. Your life will be impacted everywhere by digital information, display and electronics. We will have a piece of that change also. In many places, precious water will become more drinkable and useable and fluids more pure because of 3M. The future looks very bright for our company.

Let me speak now briefly about 2008 Guidance.

From our perspective, nothing has materially changed since our December 12 meeting in New York. Some things have worsened a little, for example, the US economy in general, but other factors have stabilized or improved such as the performance of our core businesses like Abrasives and Industrial tapes. International continues to grow very strong.

Despite what we read and hear in the press, not everything in the garden is gloomy. A few more tail winds have appeared. For example, we expect commodity prices to ease during the year, particularly some metals, wood pulp and paper, that will help ease some Gross Margin pressure. It will specifically help Consumer and Office, Industrial Minerals and our Electro and Communications businesses. Foreign exchange will also still be very positive factor in our case. Going forward, we expect M&A pricing to moderate, bringing new opportunities for growth to 3M that we might otherwise have passed up on.

We have a proven ability to execute on cost reductions due to our great Lean Six Sigma capability. And we have lower-risk business activities in security, medical and fluid treatment. Our positive outlook on oil and gas, mining and aerospace is unchanged. Together with international, we think these elements offset the increased risks in US consumer, US automotive and US housing. But even on housing, we believe that we will see the bottom of the US housing and comparisons will get easier from that time on.

This is a time when we intend to get ever stronger, to take market share from our competitors and a lot of that is available to us. We intend to make our competition feel the heat a lot more than we do.

So where does this all take us? We have stress tested our earnings numbers against various economic circumstances and believe we can deliver a minimum of 10% EPS growth even in these confused and occasionally trying circumstances. We need to keep a proper sense of perspective. The rebuilding of capability we have done on many fronts in the last two years will serve us well in this venture.

As far as the first quarter is concerned, because of the fabulous first quarter we had in 2007, the year-over-year financial comparisons will be challenging. And the period in and around the Easter holiday, which impacts business activity in both Europe and Latin America, falls in the first quarter this year, but was in the second quarter in 2007. There is also a slightly longer Chinese New Year holiday this year that will reduce sales in Asia a little. These factors will result in some shifting of sales from Q1 to Q2. Nothing fundamentally flawed here, just timing. Year-on-year comparisons get a little easier in the quarters farther out, particularly in the second half.

So we are pleased to affirm again that we will deliver 10% EPS growth in 2008. Investors should not presume we have are implying that we have exact precision on the EPS growth number either, but that the 10% is what we say it is, a minimum. From my perspective, this forecast shows the resilience and strength of 3M. We will continue to manage investments and overall costs prudently in the next year.

And with that said, we would welcome any questions you may have. Thank you very much everybody.

(Intercall announces Q&A details)