Illinois Tool Works

Flight to Quality; Assuming Coverage with OW

Overweight

$54.88
07 August 2007

Machinery Industry

Stephen Volkmann, CFA[AC]
(1-212) 622-1300
stephen.e.volkmann@jpmorgan.com

Sabina Chatterjee
(1-212) 622-2855
sabina.chatterjee@jpmorgan.com

Philip M Gresh
(1-212) 622-4861
phil.m.gresh@jpmorgan.com

We are assuming coverage of Illinois Tool Works with an Overweight rating (under previous JPM coverage, ITW was rated Overweight). In our view, ITW is one of the best-run diversified industrial manufacturers, characterized by its above-average long-term ROIC and operating margins, strong cash generating capabilities, and low EPS volatility – trading at the low end of historical ranges amid market concerns over the company's housing and auto exposure.

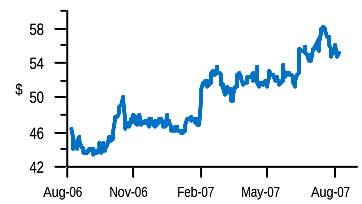
- **A high quality way to play the Diversified Industrial sector.** ITW has delivered high teens operating margins and ROIC through all economic conditions, making it among the least volatile industrial names. Earnings have grown at a 15% CAGR over the last 20 years and fell only once (15%) in that period. Total shareholder return has averaged 13%.

- **Market's focus on ITW's auto and housing sensitivity is overdone, in our view.** ITW's growth and margins have lagged some other industrial companies lately, partly due to its 20% exposure to housing and automotive markets. Looking ahead, however, comparisons in these businesses start to get easier, and restructuring should help boost margins. Note that ITW has a long history of making solid returns in these businesses in a variety of end-market conditions.

- **Recent credit jitters could help ITW.** A large part of the ITW story is the company's ability to grow through acquisitions. Though the company rarely competes with private equity for these acquisitions due to their small individual sizes, recent credit jitters could help to settle price expectations in the acquisition markets.

- **Valuation looks attractive.** ITW's current EV/Sales and EV/EBITDA of 185% and 9.5x, respectively, compare to 10-year averages of 200% and 11x. On a P/E basis, the current 16x 2007E compares to a range of 14-22x and a peer group average of 18x. As important, ITW's multiples have historically expanded as the industrial cycle slows.

Price Performance



	YTD	-1M	-3M	-12M
Absolute	19.5%	-1.1%	4.2%	19.2%

Source: RIMES, Reuters.

Illinois Tool Works (ITW;ITW US)

	2005A	2006A	2007E	2008E	2009E
EPS ($)					
Q1 (Mar)	0.53	0.65	0.71A		
Q2 (Jun)	0.64	0.81	0.90A		
Q3 (Sep)	0.72	0.78	0.88		
Q4 (Dec)	0.71	0.80	0.90		
FY	2.60	3.04	3.40	3.90	4.40

Source: Company data, Reuters, JPMorgan estimates. Data in this table reflect pricing as of 8/7/07 close. All other data and valuation reflect pricing as of 8/6/07.

Company Data	
Price ($)	54.88
Date Of Price	07 Aug 07
52-week Range ($)	58.59 - 42.96
Mkt Cap ($ bn)	31.33
Fiscal Year End	Dec
Shares O/S (mn)	571

See page 21 for analyst certification and important disclosures, including investment banking relationships.

Stephen Volkmann, CFA
(1-212) 622-1300
stephen.e.volkmann@jpmorgan.com

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Stephen Volkmann, CFA
(1-212) 622-1300
stephen.e.volkmann@jpmorgan.com

Key Investment Points

Illinois Tool Works

Overweight

A high quality way to play the Diversified Industrial sector

As the economy moderates, we believe investors need to become more selective, opting for higher quality companies with lower earnings volatility and better exposure to the long/late cycle end markets. ITW fits the bill, in our view, and is among the best candidates in our group to post consistent earnings growth in the range of 10-15% against the backdrop of a slowing North American industrial economy. During the up cycle, ITW lagged some of its diversified industrial peers (and nearly all the early cycle Machinery names) as companies more leveraged to an early-cycle recovering economy outperformed. However, the inverse has traditionally occurred as growth in the industrial economy slows – likely reflecting investor preference for higher quality names to provide better later cycle growth and greater downside protection. We believe the same phenomenon could unfold this time around. ITW's stock has lagged its peers thus far this cycle, giving investors a chance to buy this high quality (and more defensive) name at a discount to historical averages.

Please see our report, *The Later Cycle Shift Is On,* published August 8, 2007, for an overview of the Diversified Machinery industry.

Market's perception of ITW's auto and housing sensitivity may be overdone

ITW shares have lagged most of the industrial peers so far this cycle, partly as growth in the 'pure plays' has been stronger early in the cycle, and partly as investors were likely concerned with the company's exposure to the weak US auto and housing markets. While ITW does have more exposure than many Machinery peers, we believe it is less than many investors believe, and would note that the company has a history of growing these businesses even in challenging economic conditions. ITW's total exposure to these sectors combined amounts to about 20%, of which perhaps 60% is related to North America. Still, weakness in auto and housing has put some near-term pressure on ITW's margins. Looking ahead, we expect easier comparisons and restructuring actions to remove both the top and bottom line drag from these businesses, even if end-market conditions remain depressed.

Acquisition activity should set up margin expansion in 2008

Despite concerns over competition from private equity, ITW had a banner year for acquisitions in 2006, acquiring $1.7 billion in sales at a total cost of $1.5 billion – incidentally, a bit below long term average prices paid. In a more normal year, as this one appears to be, acquired revenues should be closer to $0.9 -$1.2 billion. The near term impact of last year's acquisitions has been dilutive to margins, as new businesses generally come on at half of normal 18% ITW margins and carry some step up amortization. As we look to 2008, step up accounting charges should fade at the same time that underlying margins begin to expand. Importantly, this margin expansion does not require improvement in company end markets.

ITW's Valuation Relative to Peers

	ITW			DI Peers
	Low	Hi	Current	Avg
EV/Sales	130%	290%	185%	140%
EV/EBITDA	8.0	19.0	9.5	9.5
P/E	12.5x	24.0x	16.0x	15.0x

Source: JP Morgan estimates. EV multiples on an NTM basis. DI Peers = ETN, IR, PH, KMT

EPS growth has outpaced that of the market, yet the shares only trade in line.

ITW has achieved above average earnings growth throughout the past decade. Since 1997, the company's EPS grew at a compounded annual rate of 10%, above the 7% average for companies in the S&P 500 index. Despite this outperformance, the shares are trading at a P/E of 16 times – essentially in line with the market. Using enterprise multiples, ITW's stock is trading at a discount, as EV/Sales of 185% compares to a 10 year average of 200%, while EV/EBITDA of 9.5x compares to 11x historically.

ITW also trades at a discount to similar diversified industrial peers (including multi-industry names), which trade at about 11x 2007E EBITDA and 18x P/E.

Investment Risks

Stalled base revenue growth may contain stock performance
ITW has posted a base sales increase of 1-2% (3-month rolling average) for the last ten months, likely reflecting a slowdown in the industrial economy. The company has guided to base revenue growth of 2.1-4.1% for the year, so the lack of a pickup in the near term could prevent the stock from meaningfully appreciating. However, ITW has been extremely active on the acquisition front, which should help offset tepid growth in its base businesses.

Growth at the expense of margins?
As ITW integrates new acquisitions, margins typically decline as the 80/20 principles are applied and product lines are phased out. In addition, step-up amortization generally pressures margins in the first three quarters of ownership. By the third year, most of the margin improvement is complete and sales are growing above the original acquisition level. ITW has been making more acquisitions recently, targeting $900m-$1.2b of annualized revenues in 2007 after acquiring $1.7b in 2006. Although expected to help offset lower base revenue growth, this strategy could put pressure on margins in the near term.

The economy could slow greater than expected
JPM economists expect a moderation in GDP growth from 2.9% in 2006 to 2.0% and 2.7% in 2007 and 2008, respectively. In the event the economy slows more than generally anticipated, this could inhibit ITW’s earnings growth and present increased margin pressure.

Stephen Volkmann, CFA
(1-212) 622-1300
stephen.e.volkmann@jpmorgan.com

Company Description

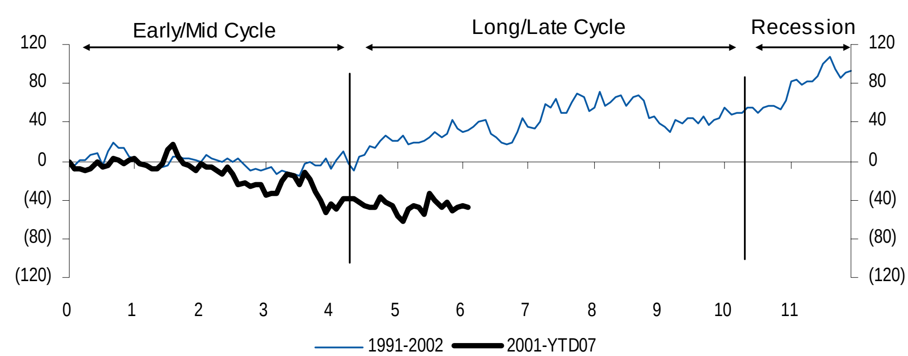
Illinois Tool Works is a global manufacturer of highly engineered products and specialty systems. The company has 750 operations in 49 countries and employed roughly 50,000 people at year-end 2006. ITW is organized under four business segments: Engineered Products North America (EPNA), Engineered Products International (EPI), Specialty Systems North America (SSNA) and Specialty Systems International (SSI). The Engineered Products segment (48% of 2006 sales) manufactures a variety of short lead-time plastic and metal components and fasteners, as well as specialty products for a diverse worldwide customer base. The Specialty Systems (52% 2006 sales) segment designs and manufactures longer lead-time machinery and related consumables, as well as specialty equipment.

A High Quality Defensive Play

As the economy moderates, we believe investors need to become more discriminating, selecting higher quality companies with better exposure to the long/late cycle end markets. ITW fits the bill, in our view, and is likely the best candidate to post consistent earnings growth in the range of 10-15% against the backdrop of a slowing North American economy. Going forward, ITW could outperform other Machinery companies as investors select high quality names that provide greater downside protection in an unexpected economic downturn.

Figure 1: ITW Outperformed Other Diversified Industrials During the Last Economic Slowdown

Difference in performance, rel to S&P, between ITW and average of ETN, IR, PH, KMT



Source: FactSet

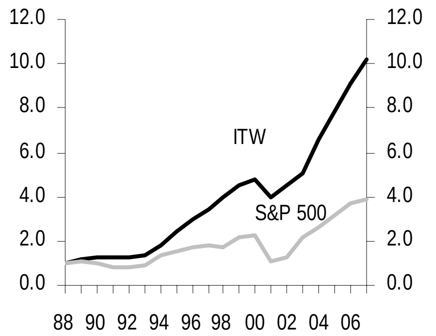
Consistently above-average EPS growth warrants a high multiple, yet shares are trading only in line with the market. Since 1997, ITW's EPS has grown at a compounded annual rate of 10%, above the 8% average for companies in the S&P 500 index. Over 20 years, ITW has grown earnings at a 15% CAGR, with only one down earnings year (~15%). As part of its five year goals, management targets continued strong EPS growth, with a compounded rate of 13-15%. Yet the shares are trading at a P/E of 16 times - essentially in line with the market, and at a discount to the diversified industrial peer group, despite the historical outperformance. The company's strong earnings track record is even more impressive considering its

Stephen Volkmann, CFA
(1-212) 622-1300
stephen.e.volkmann@jpmorgan.com

conservative accounting—including its use of above-line restructuring charges, accelerated depreciation methods, and a stringent inventory grading policy.

Figure 2: Earnings Growth Exceeds the S&P 500

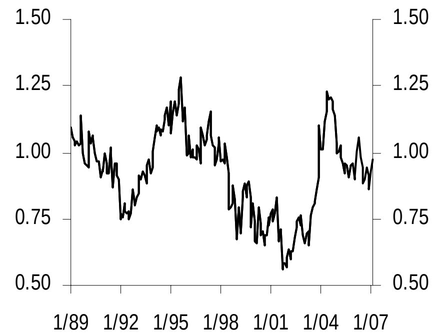
Index 1988=1.00



Source: Company reports, JPMorgan ests, FactSet.

Figure 3: ITW's P/E Relative to the S&P 500

LTM



Source: Company reports and FactSet.

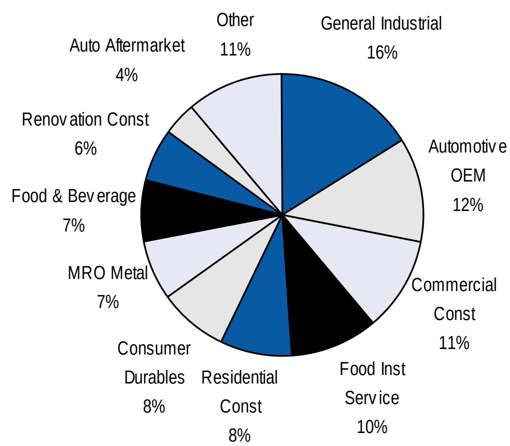
Auto and housing exposure concern is overdone

Ten years ago, ITW's revenue mix was roughly 23% automotive, with 80% of that in North America. After a decade of growth focused elsewhere, ITW's business is now about 12% automotive, with 4% of that now international. 80% of the NA auto exposure is currently Big 3, but the company expects "new domestics" to account for 35% of NA over the next several years based on programs already won. Note that foreign producers are adding significant new capacity in 2008-09 in the US. Content at the Big 3 is currently about $60-65/car, and is more like $20-25 at the new domestics, leaving significant penetration potential. ITW has historically grown its Big 3 penetration by about 4-5% per year.

Residential construction accounts for about 10% of total sales, with 5-6 percentage points in North America. Globally, construction accounts for about 22% of total sales, including some packaging equipment such as strapping for building supplies. In total, 55% of construction exposure is outside North America.

Figure 4: Auto and Housing Globally Account for Less than 20% of ITW's Sales

% of 2006 sales



Source: Company reports.

We believe that the market's focus on housing and auto is overdone for the following reasons:

- **Comparisons are easing.** Housing and auto weakness began for ITW in the 4Q 2006, and these end markets have stabilized for the company in recent months. Looking ahead, the drag on top line growth should ease as comparisons get less difficult. Note that easier comparisons are likely to be the exception rather than the rule in the industrial space over the next several quarters.

- **Restructuring should drive margin recovery.** Nearly a year into slower market conditions, ITW has had the opportunity to adjust its businesses for the end-market conditions. We expect margin improvement as these restructuring actions bear fruit into 2008.

- **Businesses have a strong track record.** Interestingly, ITW's automotive and housing businesses are among the higher return businesses in the company's portfolio, and have been through most end-market environments.

Outlook for industrial end markets is mixed, but ITW is among the best positioned to manage the coming volatility. According to ITW, general industrial slowing in the U.S. has contained base revenue growth to a range of 1-2%, which is likely sustainable through the second half of the year. The current slowdown is reflected in ISM volatility, as well as weaker business confidence. In several industrial end markets, companies are not investing in new capital equipment, but are rather using existing capacity.

For housing, ITW believes starts could bottom in the 1.5mm area and remain there for a year or so before gradually returning to the 1.7-1.8mm range over the next several years. Renovation in North America has also fallen off, reflecting less equity cash out as a result of sub-prime market issues. Commercial construction, which lags residential by 9-12 months, can be broken out by the following sub-segments:

1) Retail: still growing, albeit at a slower rate 2) Commercial warehouse: feeds into the retail market 3) Office: currently very weak 4) Manufacturing: up slightly and 5) Institutional: flat.

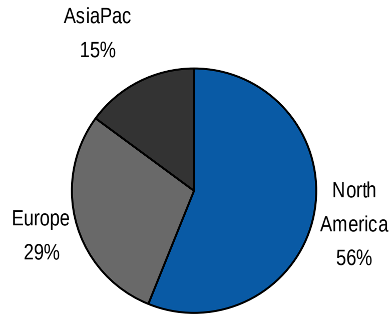
In the food equipment segment, restaurant growth has slowed to 2% from an average of 5% in recent years, in part reflecting a slowdown in the housing market. But for ITW, menu changes and service of the installed base are more important drivers of the food business. Service, which is based on long term maintenance contracts, now accounts for 30% of ITW's food business - up from 15% pre-Premark. The majority of ITW's sales are to institutions and restaurants; supermarkets once made up 30% of sales but this number has whittled to 15% as a result of Wal-Mart's effect of reducing food handling and processing at the retail supermarket.

Despite participating in these relatively mature, economically sensitive areas (automotive, housing, construction), ITW's top line growth has routinely exceeded that of its end markets. Between the company's disciplined approach to acquisitions, the 80/20 operating philosophy, continuous product enhancements and strong management, we believe ITW will be able to manage currently challenged sectors. ITW's five year growth goals consist of 10-13% CAGR over the next five years, with base revenues contributing 5-6% of that (versus 4% historically) and the remainder coming from acquisitions. This would be an improvement from the 8.6% growth posted from 2001-2006, and is expected to be achieved by investment in new products, geographic expansion and acquisitions into platforms with higher growth rates. As a result of the higher R&D spend, however, ITW does not foresee any improvement in ROIC (16-18%).

Similar to other diversified industrial names, ITW has lowered its dependence on North America. A decade ago, 65% of ITW's sales were derived domestically, with Europe and Asia accounting for 26% and 9% of revenue, respectively. That balance has shifted, as ITW ended 2006 with a 56%/29%/15% mix across those three regions. For 2010, dependence on North America is expected to further reduce, as Europe and Asia account for 30% and 20% of total sales. This favorable shift should help provide further insulation from the economically sensitive sectors of North America.

Figure 5: ITW Sales by Geography

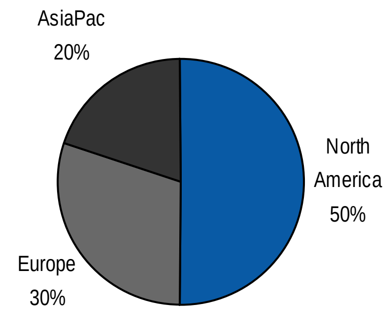
% of 2006 Sales



Source: Company reports.

Figure 6: 2010 Goals for Geographic Sales Mix

% of 2010E Sales



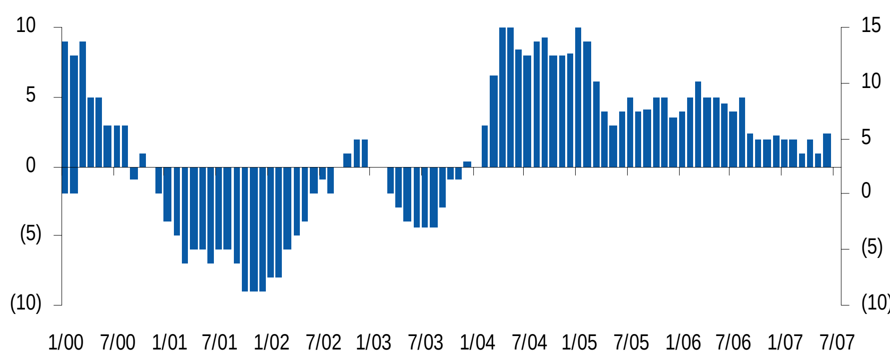
Source: Company reports.

Earnings and Cash Flow Outlook

ITW's base revenue growth has stalled as of late, with the company reporting an average increase of less than 2% (annual, based on a rolling 3-month basis) this year. The lack of significant growth is attributable to challenges in domestic markets, but acquisitions and overseas markets have kept overall revenues strong. Most recently, ITW reported total revenue growth of 13% for the 3 months ending June.

Figure 7: ITW's Base Sales Growth

yoy % chg, 3 mo rolling average



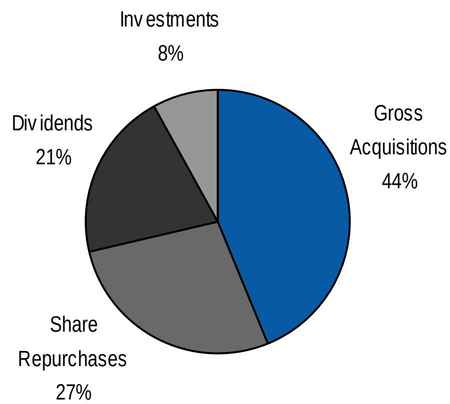
Source: Company reports.

Strong cash flow generation could support further share repurchases

ITW reported operating free cash flow near $1.8 billion at the end of 2006, and we expect levels to be in the range of $1.6-$2.0 billion over the next few years, reflecting higher earnings levels and good control of working capital. The priority for free cash flow spend remains acquisitions, with $900M-$1.2B allotted for 2007. In terms of share buybacks, ITW spent nearly $200 million in 2006, and expects to spend $700-900M in 2007. The company has also stepped up its dividends, changing its guideline to 25-35% of trailing two years net income (versus three years previously). The company noted that in the event acquisition activity accelerates, repurchases would slow, and vice versa.

Over the last decade, ITW has spent close to 50% of its free cash on acquisitions, a quarter on share repurchases (the first ever share repurchase program started in April 2004) and 20% on dividends. We expect acquisitions to remain the largest portion of free cash spend, while dividends could increase over the next few years.

Figure 8: ITW's Uses of Free Cash Flow Over the Last Decade
1997-2006



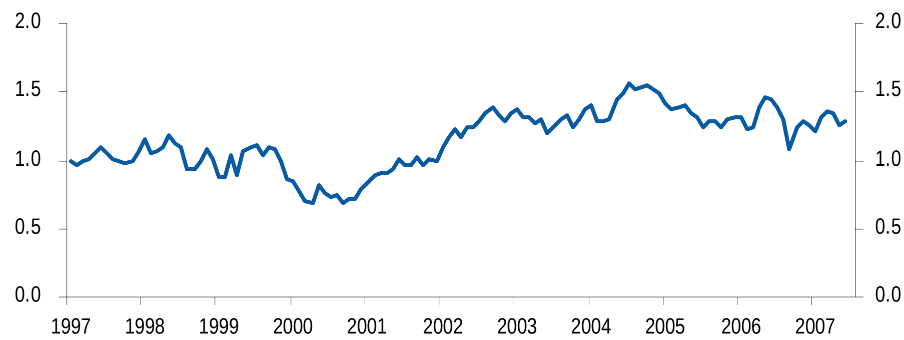
Source: Company reports and JPMorgan estimates.

Valuation

Valuation seems reasonable at current levels
We assume coverage of ITW with an Overweight rating, and believe that although the shares are trading in line with their historical average, there may be more opportunity for share appreciation. ITW's stock is up 20% thus far this year, lagging the overall group's 32% increase but well ahead of the market's 3% rise. Currently, ITW is trading at 185% of forward sales (10 year average = 200%), 9.5 times EV/EBITDA (vs average of 11x) and at 16 times 2007E earnings. On a two year forward basis, the P/E of 14.6x is below with the long term 17.4x average.

Figure 9: ITW's Stock Has Essentially Performed In Line with the Market

Jan 97=1.00, relative to S&P500

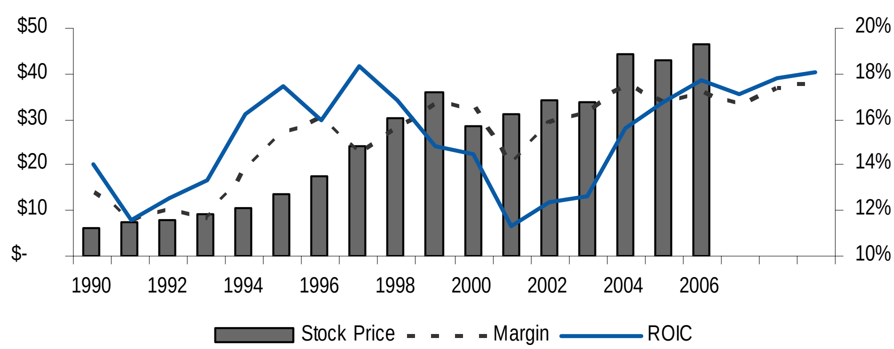


Source: Company reports and JPMorgan estimates.

ITW's stock performance has generally trended in line with return on invested capital. Going forward, we expect ROIC to plateau, although the shares could continue to appreciate given better margins.

Figure 10: ROIC Could Remain Flat After Increasing Significantly Since 2001

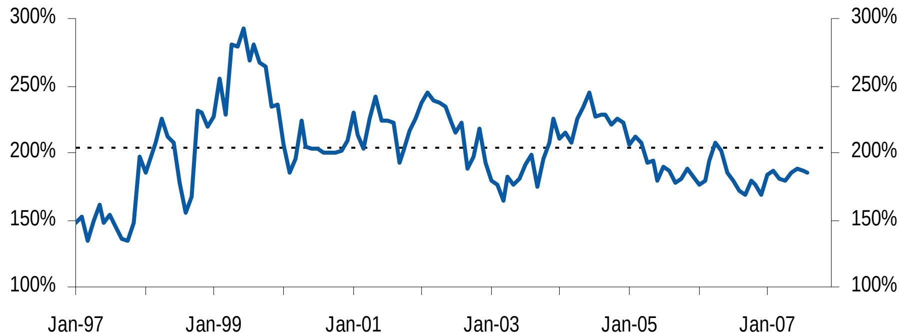
Stock price (left axis) ROIC, margin (right axis)



Source: Company reports and JPMorgan estimates.

Figure 11: On an EV/Sales Basis, ITW Stock Is Trading Below the 10 Year Average of 200%

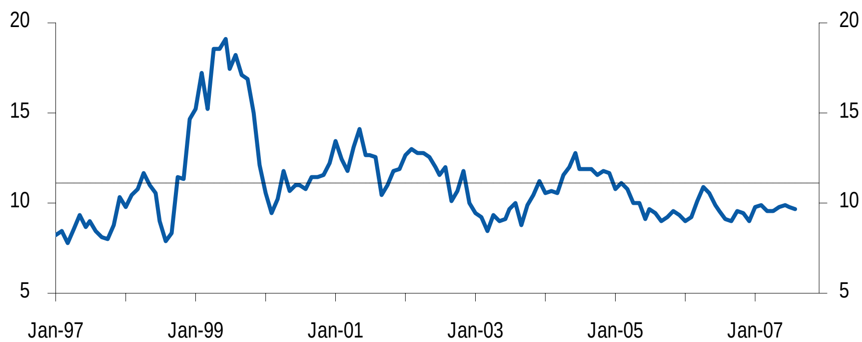
EV/Forward Sales



Source: Company reports and JPMorgan estimates.

Figure 12: Current EV/EBITDA Is Also Below the Historical Average

EV/Forward EBITDA

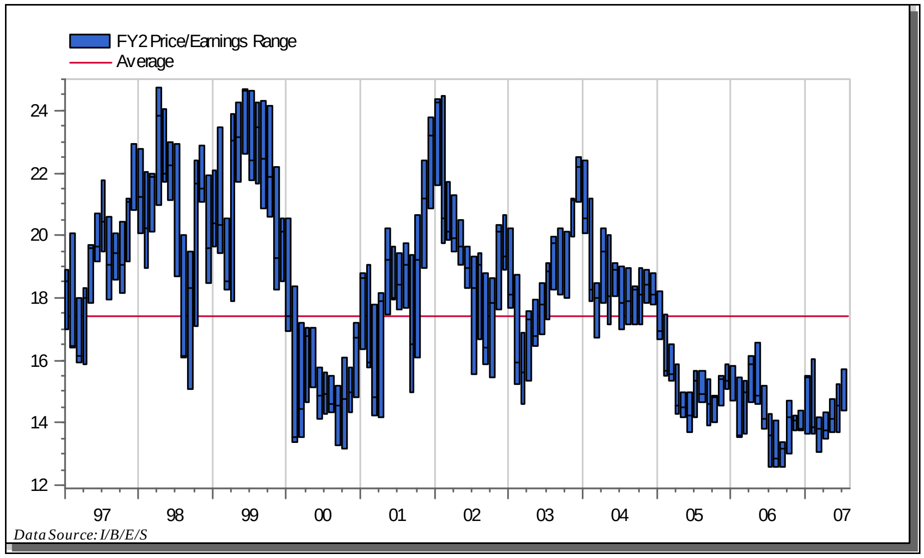


Source: Company reports and JPMorgan estimates.

Stephen Volkmann, CFA
(1-212) 622-1300
stephen.e.volkmann@jpmorgan.com

Figure 13: ITW's Price to Earnings Ratio Is Well Below Average

Based on 2 year forward EPS



Source: FactSet.

Stephen Volkmann, CFA
(1-212) 622-1300
stephen.e.volkmann@jpmorgan.com

Figure 14: ITW Annual Income Model, 2000-2009E

Illinois Tool Works **Earnings Model** *in millions except per share data*	**2000R**	**2001**	**2002**	**2003**	**2004**	**2005R**	**2006**	**2007E**	**2008E**	**2009E**	**2006**	**2007E**	**2008E**	**2009E**
Sales	$9,512	$9,293	$9,468	$10,036	$11,731	$12,790	$14,055	$16,205	$18,037	$19,750	10	15	11	10
Adjusted Cost of Sales	5,710	5,774	5,756	6,043	7,070	7,825	8,403	9,772	10,840	11,850	7	16	11	9
Adjusted Gross Profit	$3,802	$3,519	$3,711	$3,993	$4,661	$4,965	$5,652	$6,434	$7,197	$7,900	14	14	12	10
Depreciation/Amort.	273	282	278	282	294	299	319	340	360	380	7	6	6	6
Goodwill Amort.	119	105	28	24	59	84	125	110	100	100	49	(12)	(9)	0
Pension & Health	23	34	78	96	103	98	220	230	230	240	124	5	0	4
Research	106	102	101	107	123	128	135	162	165	170	6	20	2	3
Cost of Goods	$6,230	$6,296	$6,242	$6,552	$7,650	$8,434	$9,202	$10,614	$11,695	$12,740	9	15	10	9
Gross Profit	$3,281	$2,997	$3,226	$3,484	$4,081	$4,356	$4,853	$5,592	$6,342	$7,010	11	15	13	11
S G & A	1,704	1,691	1,720	1,850	2,024	2,215	2,432	2,885	3,202	3,521	10	19	11	10
Operating Profit	$1,577	$1,306	$1,506	$1,633	$2,057	$2,141	$2,421	$2,707	$3,140	$3,489	13	12	16	11
Interest Expense	70	68	68	71	69	95	86	98	100	100	(10)	14	2	0
Other Income (Expense)	(11)	(7)	(4)	13	12	135	110	85	0	0				
Pretax Income	$1,496	$1,231	$1,434	$1,576	$1,999	$2,182	$2,445	$2,694	$3,040	$3,389	12	10	13	11
Income Taxes	527	428	502	536	660	687	728	795	897	1,000	6	9	13	11
Net Income - Cont. Oper.	$969	$802	$932	$1,040	$1,340	$1,495	$1,718	$1,899	$2,143	$2,389	15	11	13	11
Unusual Items	(11)	3	(219)	(17)	(1)	0	0	0	0	0				
Final Net Income	$958	$806	$713	$1,024	$1,339	$1,495	$1,718	$1,899	$2,143	$2,389	15	11	13	11
Avg. Shares	608.8	612.6	616.1	617.5	609.6	575.4	569.9	558.5	550.2	542.5	(1)	(2)	(1)	(1)
Per Share														
Continued Oper.	$1.59	$1.31	$1.51	$1.68	$2.20	$2.60	$3.01	$3.40	$3.90	$4.40	16	13	15	13
Unusual Items	(0.02)	0.01	(0.36)	(0.03)	(0.00)	0.00	0.00	0.00	0.00	0.00				
Net EPS	$1.57	$1.32	$1.16	$1.66	$2.20	$2.60	$3.01	$3.40	$3.90	$4.40				
% of Sales														
Adjusted Gross Profit	40.0	37.9	39.2	39.8	39.7	38.8	40.2	39.7	39.9	40.0				
Gross Profit	34.5	32.3	34.1	34.7	34.8	34.1	34.5	34.5	35.2	35.5				
S G & A	17.9	18.2	18.2	18.4	17.3	17.3	17.3	17.8	17.8	17.8				
Operating Profit	16.6	14.1	15.9	16.3	17.5	16.7	17.2	16.7	17.4	17.7				
Pretax Profit	15.7	13.2	15.1	15.7	17.0	17.1	17.4	16.6	16.9	17.2				
Net Profit	10.2	8.6	9.8	10.4	11.4	11.7	12.2	11.7	11.9	12.1				
Tax Rate	35.2	34.8	35.0	34.0	33.0	31.5	29.8	29.5	29.5	29.5				
Incremental Margins	124%	114%	22%	25%	8%	22%	13%	17%	17%	18%				

Source: Company reports and JPMorgan estimates. R = Restated.

Stephen Volkmann, CFA
(1-212) 622-1300
stephen.e.volkmann@jpmorgan.com

Figure 15: ITW Annual Segment Earnings Model, 2000-2009E

Illinois Tool Works **Segment Earnings Model** *in millions except per share data*	2000R	2001	2002	2003	2004	2005R	2006	2007E	2008E	2009E	2006	2007E	2008E	2009E
EP North America	$3,184	$2,974	$3,099	$3,118	$3,377	$3,766	$4,118	$4,240	$4,500	$4,750	9	3	6	6
EP International	1,467	1,472	1,566	1,898	2,492	2,744	2,915	3,730	3,850	4,250	6	28	3	10
Engineered Products Total	*4,651*	*4,446*	*4,666*	*5,016*	*5,869*	*6,510*	*7,033*	*7,970*	*8,350*	*9,000*				
SS North America	$3,337	$3,396	$3,331	$3,301	$3,776	$4,168	$4,628	$5,150	$5,350	$5,650	11	11	4	6
SS International	1,742	1,669	1,693	1,943	2,349	2,566	2,948	3,635	4,912	5,700	15	23	35	16
Specialty Systems Total	*5,079*	*5,065*	*5,024*	*5,244*	*6,125*	*6,735*	*7,575*	*8,785*	*10,262*	*11,350*				
Total Sales	**9,730**	**9,511**	**9,690**	**10,261**	**11,995**	**13,245**	**14,608**	**16,755**	**18,612**	**20,350**				
EP North America	$610	$496	$533	$504	$573	$659	$714	$691	$756	$808	8	(3)	9	7
EP International	171	180	213	263	372	406	431	544	563	633	6	26	4	12
Engineered Products Total	*781*	*675*	*746*	*768*	*946*	*1,065*	*1,144*	*1,235*	*1,319*	*1,440*	*7*	*8*	*7*	*9*
SS North America	$560	$451	$509	$534	$668	$774	$874	$968	$1,006	$1,051	13	11	4	4
SS International	192	183	165	215	311	302	402	503	815	998	33	25	62	22
Total Profit	**$1,532**	**$1,310**	**$1,420**	**$1,517**	**$1,925**	**$2,141**	**$2,421**	**$2,707**	**$3,140**	**$3,489**	13	12	16	11
EP North America	19.2%	16.7%	17.2%	16.2%	17.0%	17.5%	17.3%	16.3%	16.8%	17.0%				
EP International	11.6	12.2	13.6	13.9	14.9	14.8	14.8	14.6	14.6	14.9				
Engineered Products Total	16.8%	15.2%	16.0%	15.3%	16.1%	16.4%	16.3%	15.5%	15.8%	16.0%				
SS North America	16.8	13.3	15.3	16.2	17.7	18.6	18.9	18.8	18.8	18.6				
SS International	11.0	11.0	9.7	11.0	13.3	11.8	13.6	13.8	16.6	17.5				
Specialty Systems Total	14.8%	12.5%	13.4%	14.3%	16.0%	16.0%	16.9%	16.8%	17.7%	18.0%				
Total Margin	15.7%	13.8%	14.7%	14.8%	16.0%	16.2%	16.6%	16.2%	16.9%	17.1%				
Segment Incrementals														
EP North America	22%	55%	30%	-153%	27%	22%	15%	-19%	25%	21%				
EP International	26%	197%	35%	15%	18%	13%	14%	14%	16%	17%				
SS North America	24%	51%	32%	6%	21%	19%	15%	10%	22%	19%				
SS International	13%	-184%	-89%	-82%	28%	27%	22%	18%	19%	15%				
Total Company:														
Sales	9,884	9,661	9,871	10,413	12,143	13,245	14,608	16,755	18,612	20,350	10	15	11	9
Less Intercompany	(387)	(368)	(369)	(378)	(412)	(454)	(553)	(550)	(575)	(600)	22	(1)	5	4
Net Sales	$9,512	$9,293	$9,468	$10,036	$11,731	$12,790	$14,055	$16,205	$18,037	$19,750	10	15	11	10
Operating Profit	1,577	1,306	1,506	1,633	2,057	2,141	2,421	2,707	3,140	3,489	13	12	16	11
Margin	16.6%	14.1%	15.9%	16.3%	17.5%	16.7%	17.2%	16.7%	17.4%	17.7%				

Source: Company reports and JPMorgan estimates

Figure 16: ITW Quarterly Earnings Model

Illinois Tool Works																
Earnings Model									2006/2005				2007/2006			
in millions except per share data	1Q06	2Q06	3Q06	4Q06	1Q07	2Q07	3Q07E	4Q07E	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE
Sales	$3,297	$3,579	$3,538	$3,641	$3,759	$4,160	$4,097	$4,190	8	9	11	12	14	16	16	15
Adjusted Cost of Sales	1,958	2,146	2,142	2,156	2,271	2,494	2,491	2,516	4	6	10	9	16	16	16	17
Adjusted Gross Profit	$1,339	$1,433	$1,396	$1,484	$1,488	$1,666	$1,606	$1,673	15	13	11	16	11	16	15	13
Depreciation/Amort.	74	77	80	89	85	88	84	83	2	3	2	20	15	14	5	(6)
Goodwill Amort.	36	25	25	39	40	40	0	30	38	62	60	44	12	61	(100)	(22)
Pension & Health	55	35	36	94	60	60	60	50	121	43	44	294	9	69	68	(47)
Research	33	34	34	34	33	34	34	61								
Cost of Goods	$2,156	$2,317	$2,317	$2,411	$2,489	$2,715	$2,669	$2,740	5	7	11	13	15	17	15	14
Gross Profit	$1,141	$1,262	$1,221	$1,229	$1,270	$1,444	$1,428	$1,449	13	13	10	9	11	14	17	18
S G & A	601	602	594	635	701	746	713	725	10	8	10	12	17	24	20	14
Operating Profit	$540	$660	$627	$594	$569	$699	$715	$724	18	18	11	7	5	6	14	22
Interest Expense	19	19	21	27	24	26	25	23								
Other Income (Expense)	10	26	36	38	27	44	10	4								
Pretax Income	$531	$666	$642	$606	$571	$717	$700	$706	15	22	7	6	7	8	9	17
Income Taxes	165	201	196	166	168	212	207	208								
Net Income - Cont. Oper.	$366	$466	$446	$439	$402	$506	$494	$498	18	25	9	10	10	9	11	13
Unusual Items	0	0	0	0	0	0	0	0								
Final Net Income	$366	$466	$446	$439	$402	$506	$494	$498								
Avg. Shares	567.7	572.0	570.9	568.2	563.3	561.2	558.4	551.0	(3)	(1)	0	1	(1)	(2)	(2)	(3)
Per Share																
Continued Oper.	$0.65	$0.81	$0.78	$0.77	$0.71	$0.90	$0.88	$0.90	22	26	9	9	11	11	13	17
Unusual Items	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00								
Net EPS	$0.65	$0.81	$0.78	$0.77	$0.71	$0.90	$0.88	$0.90								
% of Sales																
Adjusted Gross Profit	40.6	40.0	39.4	40.8	39.6	40.1	39.2	39.9								
Gross Profit	34.6	35.3	34.5	33.8	33.8	34.7	34.9	34.6								
S G & A	18.2	16.8	16.8	17.4	18.7	17.9	17.4	17.3								
Operating Profit	16.4	18.4	17.7	16.3	15.1	16.8	17.5	17.3								
Pretax Profit	16.1	18.6	18.1	16.6	15.2	17.2	17.1	16.8								
Net Profit	11.1	13.0	12.6	12.1	10.7	12.2	12.0	11.9								
Tax Rate	31.0	30.1	30.5	27.5	29.5	29.5	29.5	29.5								
Incremental Margins	33%	34%	18%	10%	6%	7%	16%	24%								

Source: Company reports and JPMorgan estimates

Figure 17: ITW Quarterly Segment Earnings Model

Illinois Tool Works Segment Earnings Model *in millions except per share data*	1Q06	2Q06	3Q06	4Q06	1Q07	2Q07	3Q07E	4Q07E	2006/2005 1Q	2Q	3Q	4Q	2007/2006 1Q	2Q	3QE	4QE
EP North America	$1,043	$1,092	$1,029	$954	$1,027	1,089	1,091	1,033	14	12	7	4	(2)	(0)	6	8
EP International	627	737	724	825	833	977	902	1,018	(3)	4	10	14	33	33	25	23
Engineered Products Total	*1,670*	*1,828*	*1,753*	*1,779*	*1,860*	*2,066*	*1,993*	*2,051*	*7*	*9*	*8*	*8*	*11*	*13*	*14*	*15*
SS North America	$1,138	$1,135	$1,164	$1,191	$1,222	1,254	1,301	1,373	13	9	10	11	7	10	12	15
SS International	630	720	759	831	783	960	942	949	7	7	19	25	24	33	24	14
Specialty Systems Total	*1,768*	*1,854*	*1,923*	*2,022*	*2,006*	*2,214*	*2,244*	*2,322*	*11*	*8*	*14*	*16*	*13*	*19*	*17*	*15*
Total Sales	**3,439**	**3,682**	**3,676**	**3,800**	**3,866**	**4,280**	**4,237**	**4,373**	**9**	**8**	**11**	**13**	**12**	**16**	**15**	**15**
EP North America	$177	$210	$181	$146	$153	$194	$182	$161	22	19	0	(7)	(13)	(7)	0	10
EP International	76	110	110	135	98	148	137	162	(10)	8	9	13	29	34	25	20
Engineered Products Total	*253*	*320*	*291*	*281*	*251*	*343*	*319*	*323*	*10*	*15*	*3*	*2*	*(1)*	*7*	*10*	*15*
SS North America	218	232	227	197	224	238	247	259	24	23	8	(1)	3	3	9	31
SS International	69	107	109	117	94	118	149	143	28	16	50	41	36	10	37	22
Total Profit	**540**	**660**	**627**	**594**	**569**	**699**	**$715**	**724**	18	18	11	7	5	6	14	22
EP North America	16.9%	19.2%	17.6%	15.3%	14.9%	17.9%	16.7%	15.6%								
EP International	12.1	15.0	15.1	16.3	11.7	15.2	15.2	15.9								
Engineered Products Total	15.1%	17.5%	16.6%	15.8%	13.5%	16.6%	16.0%	15.7%								
SS North America	19.2	20.5	19.5	16.5	18.3	19.0	19.0	18.8								
SS International	10.9	14.9	14.3	14.1	12.0	12.3	15.8	15.0								
Specialty Systems Total	16.2%	18.3%	17.5%	15.5%	15.8%	16.1%	17.7%	17.3%								
Total Margin	15.7%	17.9%	17.1%	15.6%	14.7%	16.3%	16.9%	16.6%								
Segment Incrementals																
EP North America	26%	27%	1%	-30%	140%	546%	1%	19%								
EP International	41%	34%	14%	16%	11%	16%	15%	14%								
SS North America	32%	45%	15%	-2%	7%	5%	15%	34%								
SS International	39%	33%	29%	21%	16%	4%	22%	22%								
Total Company:																
Sales	3,439	3,682	3,676	3,800	3,866	4,280	4,237	4,373	9	8	11	13	12	16	15	15
Less Intercompany	(142)	(103)	(138)	(160)	(107)	(120)	(140)	(184)	28	-6	26	28	NM	NM	NM	NM
Net Sales	$3,297	$3,579	$3,538	$3,641	$3,759	$4,160	$4,097	$4,190	8	9	11	12	14	16	16	15
Operating Profit	540	660	627	594	569	699	715	724	18	18	11	7	5	6	14	22
Margin	16.4%	18.4%	17.7%	16.3%	15.1%	16.8%	17.5%	17.3%								

Source: Company reports and JPMorgan estimates

Stephen Volkmann, CFA
(1-212) 622-1300
stephen.e.volkmann@jpmorgan.com

Figure 18: ITW Annual Cash Flow Model, 2001-2009E

Illinois Tool Works **Statement of Cash Flows** *$ in millions*	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007E**	**2008E**	**2009E**
Net Income	$958	$806	$713	$1,024	$1,339	$1,495	$1,718	$1,899	$2,143	$2,389
Depreciation/Amort.	392	386	306	307	353	383	444	450	460	480
(Inc)/Loss from disc ops	11	(3)	(3)	17	1	0	0	0	0	0
Change in def income taxes	(16)	39	(60)	204	143	70	167	0	0	0
Provision for uncollectible ac's	10	22	22	9	0	7	9	0	0	0
(Gain) loss on sale of P&E	7	11	6	7	5	4	1	0	0	0
Income from investments	(152)	(140)	(147)	(146)	(143)	(126)	(79)	0	0	0
Non-cash interest	45	43	40	19	0	0	0	0	0	0
(Gain) loss on sale of ops,affiliates	6	4	5	(5)	(0)	9	(17)	0	0	0
Other	(8)	(7)	224	36	42	62	35	50	50	50
Funds from operations	$1,254	$1,160	$1,104	$1,470	$1,741	$1,904	$2,278	$2,399	$2,653	$2,919
Working Capital Needs	*(138)*	*191*	*185*	*(102)*	*(209)*	*(57)*	*(212)*	*(541)*	*(392)*	*(534)*
Trade receivables	48	157	8	(22)	(129)	(59)	(46)	(365)	(270)	(295)
Inventories	(13)	159	72	108	(177)	104	(60)	(91)	(212)	(293)
Prepaid expenses and other assets	(51)	(19)	11	(187)	(124)	(82)	(64)	0	0	0
Accounts payable	(70)	(106)	14	(10)	32	(39)	11	29	75	37
Accrued expenses and other liabilities	(94)	(62)	(10)	47	35	35	1	(114)	0	0
Income taxes payable	11	26	87	(68)	153	(17)	(55)	0	0	0
Other	31	36	1	31	0	(0)	0	0	15	17
Net cash from Operations	**1,116**	**1,351**	**1,289**	**1,369**	**1,532**	**1,847**	**2,066**	**1,859**	**2,261**	**2,385**
Net acquisitions	(791)	(542)	23	(182)	(581)	(625)	(1,338)	(1,000)	(1,000)	(800)
Capital expenditures	(306)	(257)	(271)	(258)	(283)	(293)	(301)	(300)	(310)	(320)
Sale of fixed assets	29	20	29	29	23	34	14	20	20	25
Net proceeds from investments	62	113	(117)	(74)	21	100	342	0	0	0
Other, net	2	4	3	1	8	0	9	0	0	0
Net cash from Investing	**(1,005)**	**(662)**	**(333)**	**(484)**	**(811)**	**(784)**	**(1,274)**	**(1,280)**	**(1,290)**	**(1,095)**
Cash dividends paid	(223)	(249)	(272)	(285)	(305)	(335)	(399)	(475)	(550)	(625)
Net stock issued	25	55	44	40	(1,651)	(1,017)	(368)	(800)	(500)	(500)
Net proceeds (rpmts) of ST debt	302	(352)	(231)	(68)	134	44	195	0	0	0
Net LT debt added	(264)	(12)	228	(28)	(7)	49	(16)	800	0	0
Repurchase of treasury stock	0	0	0	0	0	0	0	0	0	0
Other, net	(0)	1	3	0	0	(7)	13	0	0	0
Net cash from Financing	($160)	($557)	($229)	($341)	($1,828)	($1,266)	($575)	($475)	($1,050)	($1,125)
Effect of FX	(33)	(1)	49	83	90	(93)	3	0	0	0
Cash inc (dec) during the year	($82)	$131	$775	$627	($1,017)	($297)	$220	$104	($79)	$165
Cash at beginning of year	$233	$151	$282	$1,058	$1,684	$667	$370	$590	$694	$615
Cash at end of year	**$151**	**$282**	**$1,058**	**$1,684**	**$667**	**$370**	**$590**	**$694**	**$615**	**$780**
Debt	1,975	1,581	1,582	976	1,125	1,211	1,418	2,218	2,218	2,218
Equity	5,401	6,041	6,649	7,874	7,628	7,547	9,018	9,642	10,735	11,999
Total Capital	7,376	7,621	8,231	8,851	8,752	8,758	10,436	11,860	12,953	14,217
Debt as % Total Capital	27%	21%	19%	11%	13%	14%	14%	19%	17%	16%
Book Value Per Share	$8.87	$9.86	$10.79	$12.75	$12.51	$13.12	$15.82	$17.26	$19.51	$22.12
Return on Average Equity	19%	14%	11%	14%	17%	20%	21%	20%	21%	21%
Operating Free Cash Flow	810	1,094	1,017	1,110	1,249	1,553	1,765	1,559	1,951	2,065

Source: Company reports and JPMorgan estimates

Figure 19: Annual Balance Sheet Model, 2002-2009E

Illinois Tool Works Balance Sheet *in millions*	2000R	2001	2002	2003	2004	2005R	2006	2007E	2008E	2009E
Current Assets										
Cash and cash equivalents	$151	$282	$1,058	$1,684	$667	$370	$590	$694	$615	$780
Trade receivables	1,583	1,450	1,500	1,721	2,055	2,098	2,471	2,836	3,106	3,401
Inventories	1,108	994	963	992	1,281	1,203	1,483	1,573	1,786	2,079
Deferred income taxes	176	197	218	218	147	169	197	197	197	197
Prepaid exp, other curr assets	250	239	137	168	172	271	466	466	466	466
Total current assets	3,268	3,163	3,875	4,783	4,322	4,112	5,206	5,765	6,169	6,922
PPE, Gross	3,890	4,104	4,206	4,561	4,937	4,851	5,409	5,709	6,019	6,339
Accumulated depreciation	2,260	2,470	2,574	2,833	3,060	3,044	3,355	3,805	4,265	4,745
Net PPE	1,630	1,634	1,631	1,729	1,877	1,807	2,053	1,903	1,753	1,593
Investments	1,001	1,325	1,406	1,086	1,201	1,195	914	914	914	914
Goodwill & other intangibles	2,413	2,739	2,625	2,799	3,193	3,679	5,139	6,139	7,139	7,939
Deferred income taxes	474	439	542	371	233	45	116	116	116	116
Other	728	523	545	426	526	608	452	452	452	452
Total Assets	**9,515**	**9,822**	**10,623**	**11,193**	**11,352**	**11,446**	**13,880**	**15,289**	**16,543**	**17,937**
Current Liabilities										
Short term debt	$426	$313	$122	$56	$204	$253	$463	$463	$463	$463
Accounts payable	438	367	417	481	604	560	708	737	812	849
Accrued expenses	783	795	865	871	959	894	1,014	900	900	900
Cash dividends payable	60	67	71	74	82	93	117	117	133	150
Income taxes payable	49	33	124	7	3	81	161	161	161	161
Other current liabilities	0	0	0	0	0	120	173	173	173	173
Total current liabilities	1,757	1,576	1,598	1,489	1,851	2,001	2,637	2,552	2,642	2,696
Long term debt	1,549	1,267	1,460	920	921	958	956	1,756	1,756	1,756
Other	808	939	915	910	952	940	1,271	1,271	1,271	1,271
Total liabilities	4,114	3,782	3,974	3,319	3,724	3,899	4,863	5,578	5,668	5,723
Common stock	3	3	3	3	3	3	6	6	6	6
Additional paid in capital	584	676	748	826	979	1,083	1,379	1,379	1,379	1,379
Retained earnings	5,214	5,765	6,202	6,937	7,964	9,112	10,407	11,831	13,424	15,188
Treasury stock	(2)	(2)	(2)	(2)	(1,731)	(2,773)	(3,221)	(4,021)	(4,521)	(5,021)
Other	(399)	(402)	(302)	110	413	122	447	447	447	447
Total stockholder's equity	5,401	6,041	6,649	7,874	7,628	7,547	9,018	9,642	10,735	11,999
Short-term Debt	$426	$313	$122	$56	$204	$253	$463	$463	$463	$463
Long-term Debt	1549	1267	1460	920	921	958	956	1756	1756	1756
Total Debt	$1,975	$1,581	$1,582	$976	$1,125	$1,211	$1,418	$2,218	$2,218	$2,218
Net Debt	1,824	1,298	524	(708)	457	841	828	1,525	1,604	1,439

Source: Company reports and JPMorgan estimates

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Illinois Tool Works (ITW) Price Chart

Source: Reuters and JPMorgan; price data adjusted for stock splits and dividends.
This chart shows JPMorgan's continuing coverage of this stock; the current analyst may or may not have covered it over the entire period.
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Stephen Volkmann, CFA
(1-212) 622-1300
stephen.e.volkmann@jpmorgan.com