UNITED STATES
Securities and Exchange Commission
Washington, D.C. 20549

FORM 10-K

[X] Annual Report Pursant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended December 25, 1998 or

[ ] Transition report pursuant to Section 13 or 15(d)of the Securities Exchange Act of 1934 for the transition period from ___________ to _____________.

Commission File No. 001-9249

Graco Inc.
(Exact name of Registrant as specified in its charter)

Minnesota	41-0285640
(State or other jurisdiction of Incorporation or organization)	(I.R.S. Employer Identification No.)

4050 Olson Memorial Highway
Golden Valley, Minnesota 55422-2332
(Address of principal executive offices) (Zip Code)

(612) 623-6000
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:
Common Stock, par value $1.00 per share
Preferred Share Purchase Rights
Shares registered on the New York Stock Exchange.

Securities registered pursuant to Section 12(g) of the Act:
None

As of March 5, 1999, 20,290,698 shares of Common Stock were outstanding.

Indicate by a check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X No .

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K [X]

The aggregate market value of approximately 16,809,038 shares held by non-affiliates of the registrant was approximately $368 million on March 5, 1999.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Company's definitive Proxy Statement for its Annual Meeting of Shareholders to be held on May 4, 1999, are incorporated by reference into Part III, as specifically set forth in said Part III.

GRACO INC.

INDEX TO ANNUAL REPORT

ON FORM 10-K

NOTE: Certain exhibits listed in the Index to Exhibits beginning on page 32, and filed with the Securities and Exchange Commission, have been omitted. Copies of such exhibits may be obtained upon written request directed to:

Treasurer
Graco Inc.
P.O. Box 1441
Minneapolis, Minnesota
55440-1441

Part I

Item 1. Business

General Information

Graco Inc. ("Graco" or "the Company") supplies technology and expertise for the management of fluids in both industrial/automotive and commercial settings. The Company helps customers solve difficult manufacturing problems, increase productivity, improve quality, conserve energy, save expensive material, control environmental emissions and reduce labor costs. Graco is the successor to Gray Company, Inc., which was incorporated in 1926 as a manufacturer of auto lubrication equipment, and became a public company in 1969.

Based in Minneapolis, Minnesota, Graco serves customers around the world in the manufacturing, processing, construction and maintenance industries. It designs, manufactures and markets systems, products and technology to move, measure, control, dispense and apply a wide variety of fluids and viscous materials.

It is Graco's strategic objective to be the highest quality, lowest cost, most responsive supplier in the world for its principal products. In working to achieve its goal to be a world-class manufacturer, Graco has organized its manufacturing operations around product focused factories which contain product-based cells. The Company continues to refine these factories as new products are introduced and new equipment is purchased with the ultimate goal of creating factories which function independently. Substantial investments in new manufacturing technology have reduced cycle time and improved quality.

Operating Segment Information

Graco's businesses are classified by management into three primary operating segments: (1) Industrial/Automotive Equipment, (2) Contractor Equipment, and (3) Lubrication Equipment. Financial information concerning these operating segments is set forth in Part II, Item 7, at page 10.

Industrial/Automotive Equipment
Graco's Industrial/Automotive Equipment segment designs and markets fluid application systems, primarily for paints, coatings, sealants and adhesives. The markets served include automotive assembly and components plants, wood products, rail, marine, aerospace, farm and construction equipment, truck, bus and recreational vehicles and approximately thirty other industries, including sanitary processing, chemical processing and printing.

Worldwide, Industrial/Automotive Equipment is sold through general and specialized distribution and integrators. These distributors promote and sell the equipment, provide expertise to customers in its application, and offer integration capabilities, on-site service and technical support.

Products for the industrial/automotive markets are manufactured by product focused factories in Rogers and Minneapolis, Minnesota, and Sioux Falls, South Dakota. Assembly of certain products for the European market is performed in Maasmechelen, Belgium.

Recent Developments. In order to strengthen the sales and profitability, Graco has recently modified the way in which it markets its products to the automotive industry. It has shifted from custom-designed systems sold directly, to pre-engineered packages and modules sold through independent distributors, integrators and robot companies. As part of these changes, the automotive engineering, manufacturing and marketing functions, previously headquartered in Plymouth, Michigan, moved to Minneapolis, Minnesota in 1998. Specialized automotive marketing personnel will continue to be responsible for identifying and developing new products for automotive plants. Since integrators, line builders and robotic companies remain key channel partners in serving the automotive market despite the move to distribution, Graco will continue to field an experienced specialized sales force to serve them.

Graco is implementing a similar shift to pre-engineered packages for other targeted industries, such as wood furniture, marine and rail, where product packages will offer increased reliability and convenience to end users. In the international arena, Graco is expanding its specialized distribution to achieve maximum coverage in these industries.

In 1998, Graco introduced the PrecisionFlo Plus(TM) in the United States and expect to expand its distribution of this product worldwide in 1999. The PrecisionFlo Plus is a sophisticated electronic control device for use in sealant and adhesive dispensing systems. It maintains a uniform volume output and the desired flow rate regardless of changes in the operating environment. Process information can be stored and later analyzed. Graco also introduced a new line of variable ratio high-pressure proportioners known as Supercats(TM), designed specifically for corrosion control in the marine industry.

Products. Products offered by the segment include high and low pressure hydraulic, electric, and air-powered pumps that pressurize and transfer paints, stains, chemicals, sealants, adhesives, food, and other viscous materials through various application devices such as air, airless, electrostatic, and high-volume-low-pressure ("HVLP") spray guns. Fluid pressures ranging from 20 to more than 6,000 pounds per square inch and flow rates from under 1 gallon to 275 gallons per minute are available. Sealant and adhesive, paint circulating packages and modules, and a complete line of parts and accessories are also offered.

Contractor Equipment

Graco's Contractor Equipment segment designs and markets professional sprayers for the application of paint, and other architectural coatings and for the high-pressure cleaning of equipment and structures. The segment offers its equipment to distributors selling to professional contractors in the painting, roofing, texture, corrosion control and line striping markets.

The equipment is sold primarily through retail stores which also sell paint and other coatings, and secondarily through general equipment distributors. Manufacturers' representatives are used to sell the Company's contractor equipment to the rental market.

Products for the contractor equipment markets are manufactured by product focused factories in Rogers, Minnesota, and Sioux Falls, South Dakota. Assembly of certain products for the European market is performed in Maasmechelen, Belgium.

Recent Developments. The Ultra(R) Max electronic airless sprayers introduced in 1998 provide a higher output and more consistent spraying pressure, convenient features such as loading handles, hose racks and built-in toolboxes, and simple maintenance through easy access to the pump and intake valve. The GMax(TM) sprayers, a new line of gas-powered airless sprayers, also introduced during 1998, have similar features. In 1999, a new line of line striping equipment, LineLazer II(TM), will be offered with higher pressure, more flow and the same ease of use.

Products. The segment's primary product lines are airless paint sprayers and associated accessories such as spray guns, filters, valves and tips, high-pressure washing sprayers and specialized spraying equipment for the application of roofing materials, texture coatings and traffic paint. Fluid pressures ranging from 5 to more than 4,000 pounds per square inch and flow rates up to 4 gallons per minute are available. Pumps are available in gas, hydraulic and air-powered models in addition to electric, increasing the flexibility of contractors in areas where electricity is not readily available. High-volume-low-pressure ("HVLP") equipment has become increasingly popular as regulation of volatile emissions has increased. Replacement and maintenance parts, such as packings, seals and hoses, which must be replaced periodically in order to maintain efficiency and prevent loss of material, are also offered for sale.

Lubrication Equipment

The Lubrication Equipment segment designs, and markets products for the lubrication and maintenance of vehicles and other equipment. Equipment which dispenses, recycles and recovers lubricants in industrial/automotive settings is also offered. The markets for the segment's products include fast oil change facilities, fleet service centers, automobile dealerships and the mining industry. The purchase of vehicle lubrication equipment is often funded by major oil companies for their lubrication product customers as a marketing tool.

Products are distributed primarily through independent distributors worldwide, which are serviced by a network of independent sales representatives. Efforts have been underway in recent years to increase the number and quality of distributors serving the mining industry.

Recent Developments. The segment has developed an automatic lubricating system which is being marketed to the mining industry where continuous operations require an on-site lubricating capability and cost pressures drive the effort to mechanize and automate the production processes.

Ongoing consolidation in the oil industry and low prices for petroleum products have caused the capital spending levels of major oil companies to decline.

Products. The Lubrication Equipment segment offers a full line of lubrication pumps (air and hydraulic-powered), meters, fluid and air pressure gauges, fluid management systems, hose reels and dispense valves. The segment sells a fluid management system for the vehicle services market, which tracks and records inventories of lubricants and the quantities dispensed. It is also developing its capability to service the mining industry with automatic lubrication systems. A complete line of parts and accessories is also offered.

Products for the Lubrication Equipment markets are manufactured by product focused factories in Minneapolis, Minnesota.

Marketing and Distribution

Graco's operations are organized to sell its full line of products in each of the major geographic markets: the Americas (North, Central and South America), Europe (includes the Middle East and Africa), and Asia Pacific. The Industrial/Automotive Equipment segment, Contractor Equipment segment, and the Lubrication Equipment segment provide worldwide marketing direction and product design and application assistance to each of these geographic markets.

Graco sells its equipment worldwide principally through independent distributors. In Japan, Korea, and Europe, Graco equipment is sold to distribution through sales subsidiaries. Manufacturers' representatives are used with the Lubrication Equipment product lines and in marketing to the rental market by the Contractor Equipment segment.

In 1998, Graco's net sales in the Americas were $299,799,000 or approximately 69 percent of the Company's consolidated net sales; in Europe net sales were $93,114,000 or approximately 22 percent; and in the Asia Pacific Region, net sales were $39,272,000 approximately 9 percent.

Consolidated backlog at December 25, 1998, was $13 million compared to $22 million at the end of 1997.

Research, Product Development and Technical Services

Graco's research, development and engineering activities are organized by operating segment. The engineering group in each segment focuses on new product design, product improvements, applied engineering and strategic technologies for its specific customer base. A dedicated support group of application engineers and technicians also provides specialized technical assistance to customers in the design and evaluation of fluid transfer and application systems. It is one of Graco's goals to generate 30 percent of each year's sales from products introduced in the prior three years. With the move of the automotive engineering group to Minneapolis, Minnesota, in the summer of 1998 and its integration into the Industrial/Automotive Equipment segment, all major research and development activities are now conducted in facilities located in Minneapolis, and Rogers, Minnesota. Total research and development expenditures were $18,213,000, $17,817,000 and $17,909,000 for 1998, 1997, and 1996, respectively.

Intellectual Property

Graco owns a number of patents and has patent applications pending both in the United States and in foreign countries, licenses its patents to others, and is licensed under patents owned by others. In the opinion of the Company, its business is not materially dependent upon any one or more of these patents or licenses. The Company also owns a number of trademarks in the United States and foreign countries, including the registered trademarks for "GRACO," several forms of a capital "G" and various product trademarks which are material to the business of the Company inasmuch as they identify Graco and its products to its customers.

Competition

Graco faces substantial competition in all of its markets. The nature and extent of this competition varies in different markets due to the diversity of the Company's products. Product quality, reliability, design, customer support and service, specialized engineering and pricing are the major competitive factors. Although no competitor duplicates all of Graco's products, some competitors are larger than the Company, both in terms of sales of directly competing products and in terms of total sales and financial resources. Graco believes it is one of the world's leading producers of high-quality specialized fluid management equipment. It is impossible, because of the absence of reliable industry-wide third-party data, to determine its relative market position.

Environmental Protection

During the fiscal year ending December 25, 1998, the amounts incurred to comply with federal, state and local legislation pertaining to environmental standards did not have a material effect upon the capital expenditures or earnings of the Company.

Employees

As of December 25, 1998, the Company employed approximately 1,864 persons on a full-time basis. Of this total, approximately 278 were employees based outside the United States, and 784 were hourly factory workers in the United States.

Item 2. Properties

As of December 31, 1998, the Company's principal operations that occupy more than 10,000 square feet were conducted in the following facilities:

Type of Facility	Location	Gross Square Footage
Owned		
Distribution/Manufacturing/Office	Rogers, Minnesota	333,000
Manufacturing/Office	Minneapolis, Minnesota	242,300
Manufacturing/Office	Minneapolis, Minnesota	202,300

Engineering/Research & Development	Minneapolis, Minnesota	138,700
Office	Plymouth, Michigan	106,000
Assembly/European Headquarters/Warehouse	Maasmechelen, Belgium	75,175
Corporate Headquarters	Golden Valley, Minnesota	73,800
Manufacturing/Office	Sioux Falls, South Dakota	55,100

Leased

Office/Warehouse	Yokohama, Japan (3 facilities)	42,525
Office	Rungis, France	12,626
Office	Neuss, Germany	41,765
Office	West Midlands, United Kingdom	16,320
Office/Warehouse	Gwangju-Gun, Korea	10,549

A 20,000 square foot building in Mississauga, Ontario, Canada was sold during the last quarter of 1998.

A 106,000 square foot building in Plymouth, Michigan and a 21,000 square foot building in Los Angeles, California are currently for sale.

The Company leases space for liaison offices in China.

Graco's facilities are in satisfactory condition, suitable for their respective uses and are sufficient and adequate to meet current needs. Manufacturing capacity met business demand in 1998. Production requirements in the immediate future are expected to be met through existing production capabilities, efficiency and productivity improvements and the use of available subcontract services.

Item 3. Legal Proceedings

The Company is engaged in routine litigation incident to its business, which management believes will not have a material adverse effect upon its operations or consolidated financial position.

Item 4. Submission of Matters to a Vote of Security Holders

No issues were submitted to a vote of security holders during the fourth quarter of 1998.

Executive Officers of the Company

The following are all the executive officers of the Company as of March 5, 1999.

George Aristides, 63, was elected Vice Chairman effective March 1, 1999. From January 1, 1996 to March 1, 1999 he was Chief Executive Officer. From 1993 to 1997 he was President. From 1993 to 1996 he was Chief Operating Officer. He joined the Company in 1973 as Corporate Controller and became Vice President and Controller in 1980. He has served as a director of the Company since 1993.

Clayton R. Carter, 60, was elected Vice President, Industrial/Automotive Equipment Division, effective December 17, 1996. From January 1, 1995, he was Vice President, Lubrication Equipment Division. He became Director, Vehicle Services Division, in February 1994. He joined the Company in 1962 and has held various sales management positions.

James A. Earnshaw, 50, was elected President and Chief Executive Officer effective March 1, 1999. From 1993 to March 1999, he was Vice President, General Manager - Worldwide Hydraulics Business, Eaton Corporation, a manufacturer and marketer of electrical and electromechanical components for a wide variety of industries and a maker of ion implanters used in manufacturing semiconductors.

James A. Graner, 54, was elected Vice President and Controller in February 1994. He became Treasurer in May 1993. Prior to becoming Assistant Treasurer in 1988, he held various managerial positions in the treasury, accounting and information systems departments. He joined Graco in 1974.

John L. Heller, 62, announced his retirement effective May 3, 1999. Mr. Heller was elected Vice President, Asia Pacific, and Latin America in 1998. From 1996 to 1997 he was Vice President, Latin America and Developing Markets. From July 1993 to December 1995, he was Senior Vice President and General Manager - Contractor Equipment Division. He became Vice President, Far East Operations and Latin America, in 1992. Prior to becoming Vice President, Far East Operations in 1984, he held various management and staff positions in sales and human resources. He joined the Company in 1972.

Dale D. Johnson, 44, was elected Vice President, Contractor Equipment Division, on May 5, 1998. Mr. Johnson was previously appointed to that position on December 17, 1996. Prior to becoming the Director of Marketing in June 1996, he held various marketing and sales positions in the Contractor Equipment Division. He joined the Company in 1976.

Roger L. King, 53, was elected Vice President and General Manager, European

Operations, effective January 4, 1996. From July 1993 to December 1995, he was Senior Vice President and General Manager - International Operations. He was Senior Vice President and Chief Financial Officer from March 1993 to July 1993, and Vice President and Treasurer from 1987 to March 1993. Prior to becoming Vice President, Treasurer and Secretary in 1980, he held the position of Treasurer and Secretary and various treasury management positions with Graco. He joined the Company in 1970.

David M. Lowe, 43, was elected to the position of Vice President, Lubrication Equipment Division, in December 1996. From February 1995 to December 1996, he was Treasurer. Prior to joining the Company in 1995, he was employed by Ecolab Inc., where he held various positions in the Treasury Department, including Manager - Corporate Finance; Director, Corporate Finance and most recently Director, Corporate Development.

Robert M. Mattison, 51, was elected Vice President, General Counsel and Secretary, in January 1992, a position which he holds today.

Charles L. Rescorla, 47, is Vice President, Manufacturing and Distribution Operations, a position to which he was elected on May 5, 1998. Mr. Rescorla was previously appointed to that position on January 1, 1995. Prior to becoming the Director of Manufacturing in March 1994, he was the Director of Engineering, Industrial/Automotive Division, a position which he assumed in 1988 when he joined the Company.

Mark W. Sheahan, 34, was elected Vice President and Treasurer on December 11, 1998. Effective December 17, 1996, he was elected Treasurer. Prior to joining the Company as Treasury Operations Manager in 1995, he was a Senior Manager with KPMG Peat Marwick LLP.

Fred A. Sutter, 38, was recently appointed Vice President, Asia Pacific and Latin America. He will fully assume Mr. Heller's responsibilities effective March 1, 1999. From March 1995 to December 1998, he was Director of Marketing. Prior to joining the Company in 1995, he held various positions with Fisher-Rosemount, most recently as Director of Marketing.

The Board of Directors elected Messrs. Aristides, Carter, Graner, Heller, Johnson, King, Lowe, Mattison, Rescorla and Sheahan on May 5, 1998, all to hold office until the next annual meeting of directors or until their successors are elected and qualify.

PART II

Item 5. Market for the Company's Common Stock and Related Stockholder Matters

Graco Common Stock. Graco common stock is traded on the New York Stock Exchange under the ticker symbol "GGG." As of March 5, 1999, there were 20,290,698 shares outstanding and 6,928 common shareholders of record, which includes nominees or broker dealers holding stock on behalf of an estimated 4,462 beneficial owners.

Quarterly Financial Information.
(In thousands, except per share amounts)

1998	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Net sales	$105,717	$115,153	$106,202	$105,113
Gross profit	51,945	58,087	53,981	55,388
Net earnings	8,947	12,765	11,073	14,478
Per common share:				
Basic net earnings	0.35	0.49	0.54	0.72
Diluted net earnings	0.34	0.48	0.53	0.70
Dividends declared	0.11	0.11	0.11	0.11
Stock price (per share)				
High	$ 31.19	$ 36.50	$ 35.31	$ 30.13
Low	22.83	29.25	24.13	19.88
Close*	30.31	34.88	23.25	29.50
Volume (# of shares)	2,499	3,478	3,350	2,756

1997	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Net sales	$ 92,099	$111,721	$101,920	$108,157
Gross profit	44,533	53,399	51,362	53,694
Net earnings	6,181	10,418	12,879	15,238
Per common share:				
Basic net earnings	0.24	0.41	0.50	0.60
Diluted net earnings	0.24	0.40	0.49	0.58
Dividends declared	0.09	0.09	0.09	0.11
Stock price (per share)				
High	$ 24.08	$ 21.25	$ 23.25	$ 26.46
Low	16.17	15.67	19.42	22.17
Close*	19.17	20.08	23.83	24.87

Volume (# of shares)	2,958	4,030	1,577	2,307

*As of the last trading day of the calendar quarter.

Item 6. Selected Financial Data

Graco Inc. & Subsidiaries (In thousands, except per share amounts)	1998	1997	1996	1995	1994
Net sales	$432,185	$413,897	$391,756	$386,314	$360,013
Net earnings	47,263	44,716	36,169	27,706	15,326
Per common share:					
Basic net earnings	$ 2.06	$ 1.75	$ 1.40	$ 1.07	$ .59
Diluted net earnings	2.01	1.71	1.38	1.06	.59
Total assets	$233,702	$264,532	$247,814	$217,833	$228,385
Long-term debt (including current portion	115,739	7,959	9,920	12,009	32,483
Redeemable preferred stock	--	--	--	--	1,474
Cash dividends declared per common share	$ 0.44	$ 0.38	$ 0.33	$ 0.30	$ 0.26

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

MANAGEMENT'S REVIEW AND DISCUSSION

Graco's net earnings of $47.3 million in 1998 are 6 percent higher than the $44.7 million earned in 1997 and are significantly higher than the $36.2 million recorded in 1996. The increases in 1998 and 1997 are primarily due to higher net sales and enhanced profit margins in both years and a lower effective tax rate in 1997.

The table below reflects the percentage relationship between income and expense items included in the Consolidated Statements of Earnings for the three fiscal years and the percentage changes in those items for such years.

	Revenue & Expense Item As a Percentage of Net Sales			Revenue & Expense Item Percentage Increase (Decrease)	
	1998	1997	1996	1998/97	1997/96
Net Sales	100.0	100.0	100.0	4	6
Cost of products sold	49.2	51.0	50.0	1	8
Product development	4.2	4.3	4.6	2	--
Selling	19.2	21.1	21.8	(5)	3
General and administrative	9.6	7.8	10.1	28	(19)
Operating profit	17.8	15.8	13.5	17	23
Interest expense	1.3	0.2	0.2	*	4
Other expense (income), net	--	0.3	(0.1)	(82)	*
Earnings before income taxes	16.5	15.3	13.4	12	20
Income taxes	5.6	4.5	4.2	28	13
Net Earnings	10.9	10.8	9.2	6	24

* Not a meaningful figure.

NET SALES

Worldwide net sales in 1998 reached a record $432.2 million, a 4 percent increase over 1997 sales of $413.9 million. Advances in local volume and price increases accounted for a 7 percent increase in sales, but the impact of the strong U.S. dollar on currency translations reduced reported sales by 3 percent. By segment, 1998 net sales were up, versus 1997 in the Contractor and Industrial/Automotive segments by 10 percent and 3 percent, respectively, while sales in the Lubrication segment were 4 percent lower.

Geographically, sales outside of the Americas represented 31 percent of total sales in 1998, compared to 33 percent in 1997. The decline was due to poor economic conditions in the Asia Pacific Region. Volume gains were achieved in the Americas in 1998 with an increase of 8 percent for the year, primarily due to strong sales in the Company's Contractor Equipment and Industrial/Automotive Equipment business segments. In Europe, local sales volume advanced 16 percent and reported sales were 14 percent higher after currency translations, with double-digit sales increases in the Industrial/Automotive Equipment and Contractor Equipment segments. In the Asia Pacific Region, sales volumes declined 20 percent primarily due to poor economic conditions in the region, and were 29 percent lower after currency translations.

Worldwide net sales in 1997 were $413.9 million, a 6 percent increase over 1996. Advances in local volume and price increases accounted for a 9 percent increase, but the impact of the strong U.S. dollar on currency translations reduced reported sales by 3 percent. The 1997 increase was due to higher sales in all regions except Asia Pacific. Sales volume in the Americas, which accounted for 67 percent of net sales, advanced 9 percent. Graco's sales outside the Americas accounted for 33 percent of total 1997 sales, and were down slightly from 1996.

Consolidated backlog at December 25, 1998, was $13 million compared to $22 million at the end of 1997 and $19 million at the end of 1996. The decline in backlog was primarily due to Graco's strategic decision to restructure its automotive business, which resulted in fewer large orders.

(In thousands)	1998	1997	1996	% Increase (Decrease) 1998/97	% Increase (Decrease) 1997/96
Segment Sales:					
Industrial/Automotive Equipment	$231,924	$226,114	$224,776	3	1
Contractor Equipment	156,535	142,400	124,392	10	15
Lubrication Equipment	43,726	45,383	42,588	(4)	7
Consolidated	$432,185	$413,897	$391,756	4	6
Geographic Sales:					
Americas	$299,799	$276,410	$252,615	8	9
Europe	93,114	82,028	78,666	14	4
Asia Pacific	39,272	55,459	60,475	(29)	(8)
Consolidated	$432,185	$413,897	$391,756	4	6

GROSS MARGINS

Gross margins, expressed as a percentage of sales, were 51 percent in 1998, compared with 49 percent in 1997. The mix of products sold, pricing, improved manufacturing efficiencies and higher sales all contributed to the enhanced gross margin. 1997 gross margins of 49 percent were down from 1996 gross margins of 50 percent. This was a result of several factors, including the mix of products sold, material cost increases and exchange rates, partially offset by improved manufacturing efficiencies.

OPERATING EXPENSES

In 1998, product development expenses increased, versus 1997, to $18.2 million. In 1997, product development costs of $17.8 million were virtually unchanged from 1996. Graco is committed to expanding its sales by making significant investments in product development.

Selling, marketing, distribution and general and administrative expenses, expressed as a percentage of sales, were 29 percent in 1998 and 1997. In 1998, overall selling expenses were lower than in 1997 due to the results of corporate restructuring initiatives. Administrative expenses were higher than 1997 levels due to significant investments in information systems and restructuring charges. In 1998, operating expenses increased by 7 percent in the Contractor segment and decreased by 16 percent in the Lubrication segment. In all segments, operating expenses decreased as a percentage of net sales. In 1997, selling, marketing, distribution and general and administrative expenses, expressed as a percentage of sales, were 29 percent, versus 32 percent in 1996. The lower expense levels in 1997 were the result of the ongoing benefits of restructuring, exchange rates, higher investment returns on employee retirement plan assets and elimination of discretionary charitable contributions. In 1997, operating expenses increased by 4 percent and 3 percent in the Lubrication and Contractor segments, respectively, and decreased 3 percent in the Industrial/Automotive segment.

FOREIGN CURRENCY EFFECTS

Foreign currency translations negatively impacted 1998 earnings before income taxes by $4.5 million when compared to 1997, and decreased 1997 earnings before income taxes by $6.2 million when compared to 1996. The reduced profits in both years were due to a strong U.S. dollar, versus other foreign currencies. Since approximately 26 percent of the Company's sales and 10 percent of its product costs are in currencies other than the U.S. dollar, a strong U.S. dollar reduces the Company's profits. Gains and losses attributable to translating the financial statements of all non-U.S. subsidiaries and the gains and losses on the forward and option contracts used to hedge these exposures, which are non-speculative, are reported in Other expense (income).

OTHER EXPENSE (INCOME)

In 1998, interest expense, net of interest income, increased to $5.4 million due to the borrowing incurred to fund the repurchase of 5.8 million shares of Graco Inc. common stock from the Trust under the Will of Clarissa L. Gray.

Other expense, net of other income, was $0.2 million in 1998 compared to other expense in 1997 of $1.1 million and other income in 1996 of $0.5 million. Other expense (income) includes, among other things, the foreign currency translation gains and losses discussed above, a $1.2 million gain from the sale of real estate in 1997, a $0.8 million favorable settlement of a legal dispute in 1997 and a $1.5 million favorable settlement of a lawsuit in 1996.

INCOME TAXES

The Company's net effective tax rate of 34 percent in 1998 is one percentage point lower than the 1998 U.S. federal tax rate of 35 percent. The increase from the 30 percent rate in 1997 is due primarily to foreign earnings being taxed at higher effective rates and the full utilization in 1997 of tax benefits associated with previously reserved foreign subsidiary net operating losses. The effective tax rate of 30 percent in 1997 was lower than the 1996 rate of 31 percent principally due to foreign earnings being taxed at lower effective rates than the U.S. rate as foreign subsidiary earnings permitted the recognition of previously reserved deferred tax benefits and previous tax filings were validated. Reconciliations of the U.S. federal tax rate to the effective rates for 1998, 1997 and 1996 are included in Note D to the Consolidated Financial Statements.

ACCOUNTING CHANGES

The one-month reporting lag of the Company's European subsidiaries was eliminated in 1998 and resulted in Europe's December 1997 net earnings being recorded as an adjustment to equity.

QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

As discussed under Foreign Currency Effects, Graco sells and purchases products and services in currencies other than the U.S. dollar. Consequently, the Company is subject to profitability risk arising from exchange rate movements.

Graco uses foreign exchange contracts to reduce risks associated with foreign currency net balance sheet positions. These contracts typically have maturities of 90 days or less, and gains or losses from changes in market value of these contracts offset foreign exchange gains and losses on the underlying balance sheet items. At December 25, 1998, the foreign currencies to which the Company had the most significant balance sheet exchange rate exposure were the Canadian dollar, Spanish peseta, Japanese yen, Italian lira, British pound, German mark, Korean won, Belgian franc and French franc. The Company does not use derivative financial instruments for trading purposes.

To evaluate its currency exchange rate risks on its foreign exchange contracts, the Company uses sensitivity analysis, which measures the impact on earnings of hypothetical changes in the value of foreign currencies to which it has exposure. At December 25, 1998, due to the short-term nature of the Company's hedging instruments, reasonably likely fluctuations in foreign currency exchange rates in the near term would not materially affect Graco's consolidated operating results, financial position or cash flows.

The Company utilizes interest rate swaps to manage its exposure to fluctuations in earnings due to changes in interest rates on its variable rate debt. At December 25, 1998, a 50 basis point increase or decrease in the market interest rates, principally LIBOR, would not materially increase or decrease interest expense or cash flows.

For further discussion of the Company's foreign currency and interest rate hedging strategy and position, see Note A to the Consolidated Financial Statements.

YEAR 2000

The Year 2000 issue is the result of computer programs that were written using two digits rather than four to define the applicable year, which could cause potential failure or miscalculation in date-sensitive software that recognizes "00" as 1900 rather than 2000.

The Company is continuing its program, begun in 1996, to ensure that all information technology systems and non-information technology (non-IT) systems will be Year 2000-compliant. The assessment phase of the Year 2000 Project has been completed. It was determined that the Company needed to modify or upgrade most of its mainframe applications, operating systems, network hardware and software and desktop hardware and software. In addition, many non-IT systems required upgrading or replacement in order to ensure proper functioning beyond the year 1999.

The mainframe modification phase involving the conversion of core business applications was completed in July 1998 and the operating systems' upgrades were completed in November 1998. The network and desktop upgrades involving the replacement of certain hardware and software is scheduled to be completed by July 1999. Further testing of all mainframe applications and databases is scheduled to continue through July 1999.

Approximately 220 non-IT applications were identified at the Company with approximately 55 percent being Year 2000-compliant as of December 1998. Non-IT applications are primarily microprocessors and other electronic controls embedded in non-computer equipment used by the Company. Teams have been assembled to ensure the successful conversion of the remaining systems. These conversions will continue into 1999.

The Company has incurred costs totaling $4.5 million, including $3.2 million in 1998, and estimates a total of an additional $2.0 million to be spent in 1999 to resolve Year 2000 issues. These costs are charged to expense as incurred and include software license fees and cost of persons assigned to the project. Incremental costs associated with Year 2000 compliance are not anticipated to result in significant increases in future operating expenses and are not expected to have a material adverse effect on the results of operations, liquidity and capital resources. Existing resources are being redeployed and other projects are being delayed to accommodate Year 2000 related projects. These delays are not expected to have a material adverse impact on future results of operations or financial condition.

Business continuation plans for critical business processes and applications are being developed. These plans include adequate staffing on-site during the Year 2000 date change to quickly repair any errant applications. In addition, in the event of any problems the Company will follow its current computer outage business continuation plans until such problems are corrected.

The Company is having discussions with, and has sent questionnaires to, its suppliers to assess their Year 2000 readiness. Information will continue to be gathered from key suppliers throughout 1999. The Company will identify alternative suppliers for those suppliers unable to supply materials due to Year 2000 issues. The Company has very few customers whose loss of business would be material to the Company. It is not aware of any Year 2000 issues with these customers that would have a material adverse impact on the Company's results.

Management believes that sufficient resources have been allocated and project plans are in place to avoid any adverse material impact on operations or operating results. However, there can be no guarantee that the Company's systems will be converted in a timely fashion and Year 2000 problems will not have an adverse effect on the Company. The Year 2000 efforts of third parties are not within the Company's control and their failure to respond to Year 2000 issues successfully could result in business disruption and increased operating costs to the Company. At the present time, it is not possible to determine whether any such events are likely to occur, or to quantify any potential impact they may have on the Company's future results of operations and financial condition.

Readers are cautioned that forward-looking statements contained in the Year 2000 discussion should be read in conjunction with the Company's disclosures under the heading Safe Harbor Cautionary Statement on the next page.

EURO CURRENCY

On January 1, 1999, 11 of the 15 member countries of the European Union adopted the euro as their common legal currency and established fixed conversion rates between their existing sovereign currencies and the euro.

The Company has harmonized its price lists in the affected countries and has updated its system to allow for invoicing in the euro. Although difficult to predict, any competitive implications on the Company's pricing and marketing strategies and any impact on existing financial instruments resulting from the euro implementation are not expected to be material to the Company's financial position, liquidity or results of operations.

OUTLOOK

Overall, we expect that 1999 will be a difficult year. We anticipate that poor economic conditions will continue in the Asia Pacific Region and Latin America. In addition, we believe that the economic growth in Europe and North America will be slower than what we have experienced the last two years. Despite these conditions, we are determined to improve our earnings per share in 1999.

Graco has changed a number of business processes in recent years that have improved its effectiveness in the markets it serves, and have increased the Company's operating margins and net profits. These efforts will continue to favorably impact margins and profits in 1999. In 1998, we restructured our automotive operations, and anticipate some short-term volatility in these sales, but improved profitability as we transition to serving the automotive industry in a new and improved manner.

We anticipate that the weakness of the U.S. dollar relative to other major currencies will have a slightly positive impact on operating margins in 1999.

SAFE HARBOR CAUTIONARY STATEMENT

The information in this Annual Report on Form 10-K contains "forward-looking statements" about the Company's expectations of the future, which are subject to certain risk factors that could cause actual results to differ materially from those expectations. These factors include economic conditions in the United States and other major world economies, currency exchange fluctuations, the results of the efforts of the Company, its suppliers and customers to avoid any adverse effect as a result of the Year 2000 issue, and additional factors identified in Exhibit 99 to the Company's Annual Report on Form 10-K for fiscal year 1998.

SHAREHOLDER ACTIONS

Periodically, the Company initiates measures aimed at enhancing shareholder value, broadening common stock ownership, improving the liquidity of its common shares and effectively managing its cash balances. A summary of recent actions follows:

- repurchase of 5.8 million shares in 1998 from Graco's largest shareholder, the Trust under the Will of Clarissa L. Gray;
- three-for-two stock splits paid in 1998 and in 1996;
- an 18 percent increase in the regular dividend in 1997; and
- a 17 percent increase in the regular dividend in 1996.

LIQUIDITY AND SOURCES OF CAPITAL

The following table highlights several key measures of asset performance.

(In thousands)	1998	1997
Cash and cash equivalents	$ 3,555	$13,523
Working capital	$48,354	$87,312
Current ratio	1.6	2.3
Average days receivables outstanding	67	75
Inventory turnover	6.3	4.9

In 1998, working capital decreased $39.0 million to $48.4 million. During the first half of 1998, Graco increased its cash balance by $20.7 million from the end of 1997. In July, the Company borrowed $158 million under a newly established $190 million five-year reducing revolving credit facility (the "Revolver") and combined the proceeds of the Revolver with available cash to repurchase 5.8 million shares from the Company's largest shareholder, the Trust under the Will of Clarissa L. Gray. As a result of strong cash flow, the amount outstanding under the Revolver was reduced to $109.5 million by the end of 1998. Receivables decreased $6 million as a result of lower sales in the fourth quarter of 1998 compared with the same period in 1997. Inventories decreased $9.9 million in 1998 as a result of several factors, including the restructuring of the Company's automotive business and branch closings in Los Angeles, California, and Toronto, Canada. Cash provided by operations was $77.1 million in 1998, versus $36.3 million in 1997 and $48.6 million in 1996. In 1998, additional cash needs were funded by bank borrowings. Significant uses of cash included the repurchase of 5.8 million shares of Graco common stock for $191 million in 1998 and capital expenditures and dividends in 1997 and 1996.

The majority of 1998 capital expenditures were for manufacturing operations and information systems.

At December 25, 1998, Graco had various lines of credit totaling $171.7 million, of which $51.9 million was unused. The Company believes that the combination of present capital resources, internally generated funds and unused financing sources are more than adequate to meet cash requirements for 1999.

Item 8. Financial Statements and Supplementary Data

RESPONSIBILITY FOR FINANCIAL REPORTING

Management is responsible for the accuracy, consistency, and integrity of the information presented in this Annual Report on Form 10-K. The consolidated financial statements and financial statement schedule have been prepared in accordance with generally accepted accounting principles and, where necessary, include estimates based upon management's informed judgment.

In meeting this responsibility, management believes that its comprehensive systems of internal control provide reasonable assurance that the Company's assets are safeguarded and transactions are executed and recorded by qualified personnel in accordance with approved procedures. Internal auditors periodically review these accounting and control systems. Deloitte & Touche LLP, independent certified public accountants, are retained to audit the consolidated financial statements, and express an opinion thereon. Their opinion is included below.

The Board of Directors pursues its oversight role through its Audit Committee. The Audit Committee, composed of directors who are not employees, meets twice a year with management, internal auditors, and Deloitte & Touche LLP to review the systems of internal control, accounting practices, financial reporting and the results of auditing activities.

INDEPENDENT AUDITORS' REPORT

Shareholders and Board of Directors, Graco Inc.
Minneapolis, Minnesota

We have audited the accompanying consolidated balance sheets of Graco Inc. and Subsidiaries (the "Company") as of December 25, 1998, and December 26, 1997, and the related statements of earnings and cash flows for each of the three years in the period ended December 25, 1998. Our audit also included the financial statement schedule listed in the Index at Item 14. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the consolidated financial statements and financial statement schedule based on our audits.

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

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Graco Inc. and Subsidiaries as of December 25, 1998, and December 26, 1997, and the results of their operations and their cash flows for each of the three years in the period ended December 25, 1998, in conformity with generally accepted accounting principles. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

/s/Deloitte & Touche LLP
Deloitte & Touche LLP
Minneapolis, Minnesota
January 18, 1999

Consolidated Statements of Earnings GRACO Inc. & Subsidiaries

(In thousands, except per share amounts)	Years Ended December 25, 1998	December 26, 1997	December 27, 1996
Net Sales	$432,185	$413,897	$391,756
Cost of products sold	212,784	210,909	195,775
Gross Profit	219,401	202,988	195,981
Product development	18,213	17,817	17,909
Selling, marketing and distribution	83,169	87,479	85,281
General and administrative	41,146	32,219	39,734
Operating Profit	76,873	65,473	53,057
Interest expense	5,319	866	831
Other expense (income), net	191	1,091	(543)
Earnings before Income Taxes	71,363	63,516	52,769
Income taxes	24,100	18,800	16,600
Net Earnings	$ 47,263	$ 44,716	$ 36,169
Basic Net Earnings per Common Share	$ 2.06	$ 1.75	$ 1.40
Diluted Net Earnings per Common Share	$ 2.01	$ 1.71	$ 1.38

See Notes to Consolidated Financial Statements.

Consolidated Balance Sheets GRACO Inc. & Subsidiaries

(In thousands, except share amounts)	December 25, 1998	December 26, 1997
Assets		
Current Assets:		
Cash and cash equivalents	$ 3,555	$ 13,523
Accounts receivable, less allowances of $4,400 in 1998 and $4,100 in 1997	80,146	86,148
Inventories	34,018	43,942
Deferred income taxes, net	12,384	11,140
Other current assets	1,217	1,539
Total current assets	131,320	156,292
Property, Plant and Equipment, at Cost:		
Land	5,343	5,083
Buildings and improvements	61,712	63,981
Manufacturing equipment	98,723	91,161
Office, warehouse and automotive equipment	31,010	30,497
Construction in progress	2,334	6,218
Total property, plant and equipment, at cost	199,122	196,940
Accumulated depreciation	(102,756)	(96,760)
Net property, plant and equipment	96,366	100,180
Other Assets	6,016	8,060
Total Assets	$ 233,702	$ 264,532
Liabilities and Shareholders' Equity		
Current Liabilities:		
Notes payable to banks	$ 14,560	$ 2,911
Current portion of long-term debt	3,157	1,796
Trade accounts payable	11,965	12,542
Salaries, wages and commissions	14,025	14,903
Accrued insurance liabilities	10,809	10,227
Income taxes payable	5,134	5,546
Other current liabilities	23,316	21,055
Total current liabilities	82,966	68,980
Long-Term Debt, Less Current Portion	112,582	6,163
Retirement Benefits and Deferred Compensation	28,841	31,880
Commitments and Contingencies		
Shareholders' Equity		
Common stock, $1 par value; 33,750,000 shares authorized; shares outstanding, 20,096,814 and 25,552,694 in 1998 and 1997, respectively	20,097	25,553
Additional paid-in capital	23,892	26,085
Retained earnings (deficit)	(35,878)	105,030
Other, net	1,202	841
Total shareholders' equity	9,313	157,509
Total liabilities and shareholders' equity	$ 233,702	$ 264,532

See Notes to Consolidated Financial Statements.

Consolidated Statements of Cash Flows GRACO Inc. & Subsidiaries

(In thousands)	Years Ended December 25, 1998	December 26, 1997	December 27, 1996
Cash Flows from Operating Activities:			
Net earnings	$ 47,263	$ 44,716	$ 36,169
Adjustments to reconcile net earnings to net cash provided by operating activities:			
Depreciation and amortization	13,736	13,494	12,658
Deferred income taxes	(593)	(358)	781
Change in:			
Accounts receivable	6,293	(7,804)	(10,192)
Inventories	10,547	(3,860)	(394)
Trade accounts payable	(761)	(839)	459
Salaries, wages and commissions	(934)	437	1,081
Retirement benefits and deferred compensation	(3,255)	(626)	928
Other accrued liabilities	2,695	(8,549)	6,963
Other	2,118	(330)	148
Net cash provided by operating activities	77,109	36,281	48,601
Cash Flows from Investing Activities:			
Property, plant and equipment additions	(11,962)	(20,109)	(30,038)
Proceeds from sale of property, plant and equipment	2,201	1,990	1,058
Net cash used in investing activities	(9,761)	(18,119)	(28,980)
Cash Flows from (for) Financing Activities:			
Borrowing on notes payable and lines of credit	65,869	44,033	15,890
Payments on notes payable and lines of credit	(54,376)	(44,460)	(16,657)
Borrowings on long-term debt	180,985	--	--
Payments on long-term debt	(73,273)	(1,455)	(1,652)
Common stock issued	4,876	3,260	2,525
Retirement of common stock	(190,899)	(6,971)	(8,115)
Cash dividends paid	(10,701)	(9,608)	(8,344)
Net cash used in financing activities	(77,519)	(15,201)	(16,353)
Effect of exchange rate changes on cash	203	4,027	1,624
Net increase (decrease) in cash and cash equivalents	(9,968)	6,988	4,892
Cash and cash equivalents			
Beginning of year	13,523	6,535	1,643
End of year	$ 3,555	$ 13,523	$ 6,535

See Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
GRACO Inc. & Subsidiaries
Years Ended December 25, 1998, December 26, 1997 and December 27, 1996

A. Summary of Significant Accounting Policies

Fiscal Year. The Company's fiscal year is 52 or 53 weeks, ending on the last Friday in December.

Basis of Statement Presentation. The Consolidated Financial Statements include the accounts of the parent company and its subsidiaries after elimination of all significant intercompany balances and transactions. As of December 25, 1998, all subsidiaries are 100 percent owned. The Company's European subsidiaries' fiscal years ended December 25, 1998, and November 30, 1997 and 1996. The European subsidiaries' one-month reporting lag was eliminated in 1998 with Europe's December 1997 net earnings being recorded as an adjustment to equity. All other subsidiaries outside North America have been included principally on the basis of fiscal years ended November 30 to effect more timely consolidated financial reporting. The U.S. dollar is the functional currency for all foreign subsidiaries.

Accounting Estimates. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash Equivalents. All highly liquid investments with a maturity of three months or less at the date of purchase are considered to be cash equivalents.

Inventory Valuation. Inventories are stated at the lower of cost or market. The last-in, first-out (LIFO) cost method is used for valuing all U.S. inventories. Inventories of foreign subsidiaries are valued using the first-in, first-out (FIFO) cost method.

Currency Hedges. The Company periodically evaluates its monetary asset and liability positions denominated in foreign currencies. The Company enters into forward contracts, borrowings in various currencies or options, in order to hedge its net monetary positions. Consistent with financial reporting requirements, these hedges and net monetary positions are recorded at current market values and the gains and losses are included in Other expense (income). The Company believes it uses strong financial counterparts in these transactions and that the resulting credit risk under these hedging strategies is not significant. The notional amounts (which may not be indicative of credit or market risk) of such contracts were (in U.S. dollars) $18,717,000 and $28,271,000, and their fair value was not materially different than the notional value at December 25, 1998, and December 26, 1997, respectively.

Interest Rate Hedges. The Company utilizes interest rate swaps to convert all or a portion of its underlying debt from a variable rate to a fixed rate. Consistent with financial reporting requirements, the gains and losses on these agreements are included in interest expense. The notional amounts of such contracts were $78 million and $3.5 million at December 25, 1998, and December 26, 1997, respectively.

Property, Plant and Equipment. For financial reporting purposes, plant and equipment are depreciated over their estimated useful lives, primarily by using the straight-line method as follows:

Buildings and improvements	10 to 30 years
Leasehold improvements	3 to 10 years
Manufacturing equipment and tooling	3 to 10 years
Office, warehouse and automotive equipment	4 to 10 years

Revenue Recognition. Revenue is recognized on large contracted systems using the percentage-of-completion method of accounting. The Company recognizes revenue on other products when title passes, which is usually upon shipment.

Earnings Per Common Share. The Company adopted Statement of Financial Accounting Standards ("SFAS") No. 128, "Earnings per Share," in February 1997, which requires the presentation of earnings per share on a basic and diluted basis. Basic earnings per share is computed by dividing earnings available to common shareholders by the weighted average number of shares outstanding during the year. Diluted earnings per share is computed after giving effect to the exercise of all dilutive outstanding option grants.

Stock-Based Compensation. SFAS No. 123, "Accounting for Stock-Based Compensation," requires companies to measure employee stock compensation plans based on the fair value method of accounting. However, the statement allows the alternative of continued use of Accounting Principles Board Opinion ("APBO") No. 25, "Accounting for Stock Issued to Employees," with pro forma disclosure of net income and earnings per share determined as if the fair value method had been applied in measuring compensation cost. The Company elected the continued use of APBO No. 25.

Comprehensive Earnings. Comprehensive earnings is a measure of all nonowner changes in shareholders' equity and includes such items as net earnings, certain foreign currency translation items, minimum pension liability adjustments and changes in the value of available-for-sale securities. In 1998, 1997 and 1996, comprehensive earnings for the Company was equivalent to net earnings as reported.

Derivative Instruments and Hedging Activities. SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," was issued in June 1998 and establishes accounting and reporting standards for derivative instruments. The statement requires recognition of all derivatives as either assets or liabilities in the statement of financial position measured at fair value and will be effective in fiscal Year 2000. The Company has not yet completed its analysis of the impact SFAS No. 133 will have on its consolidated financial statements.

B. Segment Information

The Company adopted SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information," in 1998, which changes the way the Company reports information about its operating segments. The information for 1997 and 1996 has been restated to conform to the 1998 presentation.

The Company has three reportable segments: Industrial/Automotive, Contractor and Lubrication. The Industrial/Automotive segment markets fluid application systems and equipment for paints, coatings, sealants and adhesives for automotive and truck assembly and feeder plants as well as the wood products, rail, marine, aerospace, farm, construction, bus and recreational vehicles, and various other industries. The Contractor segment markets sprayers for architectural coatings for painting, roofing, texture, corrosion control and line striping and also high-pressure washers. The Lubrication segment markets products to move and dispense lubricants for fast oil change facilities, fleet service centers, automobile dealerships and mining. All segments market parts and accessories for their products.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies. The cost of manufacturing for each segment is based on product cost, and expenses are based on actual costs incurred along with cost allocations of shared and centralized functions. Certain products are sold across segments, in which case the segment marketing the product is credited with the sale. Assets of the Company are not tracked along reportable segment lines.

Reportable segments are defined by product and type of customer. Segments are responsible for the sales, marketing and development of their products and market channel. This allows for focused marketing and efficient product development. The segments share common purchasing, manufacturing and distribution.

(In thousands) Reportable Segments	Industrial/ Automotive	Contractor	Lubrication	Total
1998				
Net sales to unaffiliated customers	$231,924	$156,535	$43,726	$432,185
Segment operating profit	42,973	35,836	8,829	87,638
1997				
Net sales to unaffiliated customers	226,114	142,400	45,383	413,897
Segment operating profit	36,146	27,947	5,603	69,696
1996				
Net sales to unaffiliated customers	224,776	124,392	42,588	391,756
Segment operating profit	35,436	22,356	5,034	62,826

Profit Reconciliation	1998	1997	1996
Total profit for reportable segments	$ 87,638	$ 69,696	$ 62,826
Unallocated corporate expenses	(10,765)	(4,223)	(9,769)
Total operating profit	$ 76,873	$ 65,473	$ 53,057

Geographic Information	1998	1997	1996
Sales			
United States	$264,326	$243,197	$222,639
Other countries	167,859	170,700	169,117
Total	$432,185	$413,897	$391,756
Long-lived assets			
United States	$ 91,068	$ 94,599	$ 89,092
Other countries	10,123	11,709	12,820
Total	$101,191	$106,308	$101,912

Sales to Major Customers

No customer represented 10 percent or more of consolidated sales in the years reported.

C. Inventories

Major components of inventories for the last two years were as follows:

(In thousands)	1998	1997
Finished products and components	$27,764	$38,290
Products and components in various stages of completion	23,024	25,320
Raw materials	18,970	16,715
	69,758	80,325
Reduction to LIFO cost	(35,740)	(36,383)
Total	$34,018	$43,942

Inventories valued under the LIFO method were $22,874,000 and $26,593,000 for 1998 and 1997, respectively. All other inventory was valued on the FIFO method.

In 1998 and 1997, certain inventory quantities were reduced, resulting in liquidation of LIFO inventory quantities carried at lower costs from prior years. The effect on net earnings was not significant.

D. Income Taxes

Earnings before income tax expense consist of:

(In thousands)	1998	1997	1996
Domestic	$61,709	$53,139	$33,844
Foreign	9,654	10,377	18,925
Total	$71,363	$63,516	$52,769

Income tax expense consists of:

(In thousands)	1998	1997	1996
Current:			
Domestic:			
Federal	$17,374	$11,729	$10,518
State and local	1,600	1,709	1,201
Foreign	5,628	5,281	4,638
	24,602	18,719	16,357
Deferred:			
Domestic	(423)	1,994	(227)
Foreign	(79)	(1,913)	47
	(502)	81	243
Total	$24,100	$18,800	$16,600

Income taxes paid were $22,922,000, $17,148,000 and $14,967,000 in 1998, 1997 and 1996, respectively.

A reconciliation between the U.S. federal statutory tax rate and the effective tax rate is as follows:

	1998	1997	1996
Statutory tax rate	35%	35%	35%
Foreign earnings with (lower) higher tax rates	(1)	(3)	2
Reduction of valuation allowance	--	(3)	(6)
State taxes, net of federal effect	2	2	2
U.S. general business tax credits	(1)	(1)	(1)
Other	(1)	--	(1)
Effective tax rate	34%	30%	31%

Deferred income taxes are provided for all temporary differences between the financial reporting and the tax basis of assets and liabilities. The deferred tax assets (liabilities) resulting from these differences are as follows:

(In thousands)	1998	1997
Inventory valuations	$ 3,463	$ 3,299
Insurance accruals	3,349	3,445
Vacation accruals	1,258	1,343
Bad debt reserves	1,243	1,109
Net operating loss carryforward	606	--
Other	2,465	1,944
Current	12,384	11,140
Unremitted earnings of consolidated foreign subsidiaries	(2,827)	(3,500)
Excess of tax over book depreciation	(6,237)	(5,594)
Postretirement benefits	5,230	5,149
Pension and deferred compensation	4,428	5,397
Other	597	480
Non-current	1,191	1,932
Net deferred tax assets	$ 13,575	$13,072

1 Payable at the time these earnings are distributed to the parent, however, tax planning strategies may mitigate this liability.

Net non-current deferred tax assets above are included in Other Assets. Total deferred tax assets were $22,993,000 and $22,522,000, and total deferred tax liabilities were $9,418,000 and $9,450,000 on December 25, 1998, and December 26, 1997, respectively.

E. Debt

(In thousands)	1998	1997
Reducing revolving credit facility, 6.28% at December 25, 1998	$109,509	$ --
Industrial development refunding revenue bonds, 4.15% at December 25, 1998, payable through 2002 (property carried at $2,681 pledged as collateral)	3,000	3,500
Other	3,230	4,459
Total long-term debt	115,739	7,959
Less current portion	3,157	1,796
Long-term portion	$112,582	$ 6,163

======== =======

Aggregate annual scheduled maturities of long-term debt for the next five years are as follows: 1999-$3,157,000; 2000-$1,215,000; 2001-$1,310,000; 2002-$2,550,000; 2003-$107,507,000. Interest paid on debt during 1998, 1997, and 1996 amounted to $4,742,000, $856,000 and $841,000, respectively. The fair value of the Company's long-term debt at December 25, 1998, and December 26, 1997, is not materially different than its recorded value.

In July 1998, the Company entered into a five-year $190 million reducing revolving credit facility (the "Revolver") with a syndicate of ten banks including the lead bank, U.S. Bank National Association. The Revolver was subsequently reduced to $147 million by December 25, 1998. The Company's initial borrowing of $158 million financed a portion of the stock repurchase discussed in Note F. The $109,509,000 outstanding balance bears underlying interest at the London Interbank Offered Rate plus a spread of 0.625 percent. This spread reduces as the ratio of total debt to earnings before interest, taxes and depreciation and amortization declines. The Revolver specifies quarterly reductions of the maximum amount of the credit line, and requires the Company to maintain certain financial ratios as to net worth, cash flow leverage and fixed charge coverage. The Revolver effectively restricts dividend payments that would cause a violation of the tangible net worth ratio covenant. The amount of the restriction was $18 million at December 25, 1998.

The Company has an interest rate swap agreement in place whereby it fixed the underlying interest rate on $75 million of the Revolver at 5.74 percent through 2000. At December 25, 1998, the contractual underlying variable interest rate under the Revolver was 5.66 percent. The cash flows related to the swap agreement are recorded as income when received and expense when paid. Market and credit risk are not significant.

The Company also has an interest rate swap agreement in place whereby it fixed the interest rate of the remaining principal amounts of the Company's previously variable interest rate revenue bond debt at 4.38 percent through 2002. At December 25, 1998, the contractual variable interest rate under the revenue bonds was Bankers Trust reference rate plus 0.30 percent, or 4.15 percent.

On December 25, 1998, the Company had lines of credit with U.S. and foreign banks of $171,655,000, including the $147,000,000 Revolver. The unused portion of these credit lines was $51,889,000 at December 25, 1998. Borrowing rates under these facilities vary with the prime rate, rates on domestic certificates of deposit and the London interbank market. The weighted short-term borrowing rates were 6.3 percent, 5.8 percent and 3.6 percent at December 25, 1998, December 26, 1997, and December 27, 1996, respectively. The Company pays commitment fees of up to 0.25 percent per annum on the daily average unused amounts on certain of these lines. No compensating balances are required.

The Company is in compliance with the covenants of its debt agreements.

F. Shareholders' Equity

Changes in shareholders' equity accounts are as follows:

(In thousands)	1998	1997	1996
Common Stock			
Balance, beginning of year	$ 25,553	$ 17,047	$ 17,265
Stock split	--	8,516	--
Shares issued	344	250	188
Shares repurchased	(5,800)	(260)	(406)
Balance, end of year	20,097	25,553	17,047
Additional Paid-In Capital			
Balance, beginning of year	26,085	22,254	20,397
Shares issued	4,535	4,171	2,337
Shares repurchased	(6,728)	(340)	(480)
Balance, end of year	23,892	26,085	22,254
Retained Earnings (deficit)			
Balance, beginning of year	105,030	85,232	64,949
Net income	47,263	44,716	36,169
Dividends declared	(10,102)	(10,033)	(8,657)
Change in accounting period	300	--	--
Stock split	--	(8,516)	--
Shares repurchased	(178,369)	(6,369)	(7,229)
Balance, end of year	(35,878)	105,030	85,232
Other, Net			

Balance, end of year	1,202	841	1,517
Total Shareholders' Equity	$ 9,313	$157,509	$126,050

In July 1998 the Company repurchased 5.8 million shares of common stock for $190,887,000 from its largest shareholder, the Trust under the Will of Clarissa L. Gray. The stock repurchase was funded with cash of $32,887,000 and $158,000,000 from the Revolver discussed in Note E.

The Board of Directors declared a three-for-two stock split on December 12, 1997, in the form of a 50 percent stock dividend payable February 4, 1998; the dividend was payable to shareholders of record on January 7, 1998. Accordingly, the December 26, 1997, balance reflects the split with an increase in common stock and reduction in retained earnings of $8,516,000. All stock option, share and per share data has been restated to reflect the split.

At December 25, 1998, the Company had 22,549 authorized, but not issued, cumulative preferred shares. The Company also has authorized, but not issued, a separate class of 3 million shares of preferred stock, $1 par value.

The Company maintains a plan in which one preferred share purchase right ("Right") exists for each common share of the Company. Each Right will entitle its holder to purchase one one-hundredth of a share of a new series of junior participating preferred stock at an exercise price of $80, subject to adjustment. The Rights are exercisable only if a person or group acquires beneficial ownership of 20 percent or more of the Company's outstanding common stock. The Rights expire in March 2000 and may be redeemed earlier by the Board of Directors for $.01 per Right.

G. Stock Option and Purchase Plans

Stock Option Plans. The Company has a Long-Term Stock Incentive Plan, under which a total of 5,212,500 common shares have been reserved for issuance, with 2,830,527 shares remaining reserved at December 25, 1998. Grants under this Plan are in the form of restrictive share awards and stock options. Restrictive share awards of 963,914 common shares have been made to certain key employees under the Plan, with 52,500 shares still restricted for disposition. Such restrictions will lapse in 1999. Compensation cost charged to operations for the restricted share awards was $362,000, $188,000 and $256,000 in 1998, 1997 and 1996, respectively. In 1997, certain officers of the Company agreed to forfeit certain stock appreciation rights under an agreement which had been granted in prior years. The net impact on earnings before income taxes in 1997 was $898,000. Unearned compensation expense relating to the remaining restricted shares is $614,000 at December 25, 1998 and is included as a reduction of shareholders' equity in the Other, net category.

Stock options for 2,686,155 common shares have also been granted under the Plan. The option price is the market price at the date of grant. Options become exercisable at such time and in such installments as set by the Company, and expire ten years from the date of grant.

In 1996, the shareholders approved a Nonemployee Director Stock Option Plan, under which the Company makes initial and annual grants to the nonemployee directors of the Company. There are 300,000 common shares authorized for issuance under the Plan, all of which remained reserved at the end of 1998. Nonemployee directors receive an initial option grant of 3,000 shares upon first appointment or election and an annual option grant of 2,250 shares. The exercise price of each option is the fair market value at the date of grant. The options have a ten-year duration and may be exercised in equal installments over four years, beginning one year from the date of grant.

Options on common shares granted and outstanding, as well as the weighted average exercise price, are shown below:

	Shares	Weighted Average Exercise Price
Outstanding, December 29, 1995	1,055,795	$ 9.13
Granted	105,039	13.10
Exercised	(43,680)	8.02
Canceled	(54,362)	8.09
Outstanding, December 27, 1996	1,062,792	9.56
Granted	237,000	19.51
Exercised	(80,961)	21.46
Canceled	(115,113)	10.92
Outstanding, December 26, 1997	1,103,718	11.65
Granted	319,750	29.79
Exercised	(142,055)	8.60
Canceled	(99,625)	17.84
Outstanding, December 25, 1998	1,181,788	$16.29

The number of stock options exercisable was 510,886, 460,146 and 349,094, at December 25, 1998, December 26, 1997 and December 27, 1996, respectively. These stock options had a weighted average exercise price per share of $9.88, $8.73 and $7.97 at December 25, 1998, December 26, 1997 and December 27, 1996, respectively.

The outstanding options at December 25, 1998, expire from 2002 to 2008, with a weighted average contractual life remaining of 7.0 years, at exercise prices ranging from $6.89 to $34.81.

Stock Purchase Plans. Under the Company's Employee Stock Purchase Plan, 5,850,000 common shares have been reserved for sale to employees, 1,069,769 of which remained unissued at the end of 1998. The purchase price of the shares under the Plan is the lesser of 85 percent of the fair market value on the first day or the last day of the Plan year.

In 1994, the shareholders approved a Nonemployee Director Stock Plan which enables individual nonemployee directors of the Company to elect to receive or defer all or part of a director's annual retainer in the form of shares of the Company's common stock instead of cash. The Company issued 3,357, 2,725 and 2,282 shares under this plan during 1998, 1997 and 1996, respectively. The expense related to this plan is not significant.

Stock-Based Compensation. The Company applies Accounting Principles Board Opinion No. 25 and related interpretations in accounting for its stock option and purchase plans. Accordingly, no compensation cost has been recognized for the Employee Stock Purchase Plan and stock options granted under the Long-Term Incentive Plan and the Nonemployee Director Stock Option Plan. Had compensation cost for the stock option plans been determined based upon fair value at the grant date for awards under these plans consistent with the methodology prescribed under SFAS No. 123, "Accounting for Stock-Based Compensation," the Company's net earnings and earnings per share would have been reduced as follows:

	1998	1997	1996
Net earnings			
As reported	$47,263	$44,716	$36,169
Pro forma	45,144	43,358	35,276
Net earnings per common share			
Basic as reported	$ 2.06	$ 1.75	$ 1.40
Diluted as reported	2.01	1.71	1.38
Pro forma basic	1.97	1.70	1.36
Pro forma diluted	1.92	1.66	1.34

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions used for grants in 1998, 1997 and 1996, respectively; dividend yields of 1.5 percent, 2.0 percent and 2.9 percent; expected volatility of 40.2 percent, 32.0 percent and 25.1 percent; risk-free interest rates of 5.5 percent, 6.6 percent and 6.3 percent; and expected lives of an average of 8 years. Based upon these assumptions, the weighted average fair value at grant date of options granted during 1998, 1997 and 1996 was $12.37, $10.47 and $5.25, respectively.

The SFAS No. 123 weighted average fair value of the employees' purchase rights under the Employee Stock Purchase Plan was estimated on the date of grant using the Black-Scholes option-pricing model with the following assumptions for 1998, 1997 and 1996, respectively; dividend yields of 1.5 percent, 1.7 percent and 2.4 percent; expected volatility of 40.2 percent, 31.7 percent and 25.1 percent; risk-free interest rate of 5.5 percent, 6.5 percent and 6.1 percent; and expected lives of 1 year. The benefit of the 15 percent discount from the lesser of the fair market value per common share on the first day and the last day of the Plan year was added to the fair value of the employees' purchase rights determined using Black-Scholes. The weighted average fair value per common share was $7.85, $8.05 and $4.67 in 1998, 1997 and 1996, respectively.

H. Commitments and Contingencies

Lease Commitments. Aggregate annual rental commitments at December 25, 1998, under operating leases with noncancelable terms of more than one year, were $6,266,000, payable as follows:

(In thousands)	Buildings	Vehicles & Equipment	Total
1999	$1,808	$1,277	$3,085
2000	1,502	571	2,073
2001	725	180	905
2002	70	82	152
2003	25	26	51
Thereafter	-	-	-
Total	$4,130	$2,136	$6,266

Total rental expense was $3,307,000 for 1998, $3,339,000 for 1997 and $3,815,000 for 1996.

Contingencies. The Company is party to various legal proceedings arising in the normal course of business activities, none of which, in management's opinion, is expected to have a material adverse impact on the Company's consolidated results of operations or its financial position.

I. Retirement Benefits

The Company has a defined contribution plan, under Section 401(k) of the Internal Revenue Code, which provides additional retirement benefits to all U.S. employees who elect to participate. The Company matches employee contributions at a 100 percent rate, up to 3 percent of the employee's compensation. Prior to 1998, the Company matched employee contributions at a 50 percent rate, up to 3 percent of the employee's compensation. Employer contributions were $1,989,000, $941,000 and $841,000 in 1998, 1997 and 1996, respectively.

The Company's postretirement medical plan provides certain medical benefits for retired employees. U.S employees are eligible for these benefits upon retirement and fulfillment of other eligibility requirements as specified by the plan.

The Company has noncontributory defined benefit pension plans covering substantially all U.S. employees and directors and most of the employees of the Company's non-U.S. subsidiaries. For the U.S. plans, the benefits are based on years of service and the highest five consecutive years' earnings in the ten years preceding retirement. In 1998, the Company amended the plans to remove the 30-year limitation on benefit service. The Company funds these plans annually in amounts consistent with minimum funding requirements and maximum tax deduction limits and invests primarily in common stocks and bonds, including the Company's common stock. The market value of the plan's investment in the common stock of the Company was $19,995,000 and $16,860,000 at December 25, 1998, and December 26, 1997, respectively. The following tables provide a reconciliation of the changes in the plans' benefit obligations and fair value of assets over the periods ending December 25, 1998 and December 26, 1997, and a statement of the funded status as of the same dates.

	Pension Benefits		Other Benefits	
(In thousands)	1998	1997	1998	1997
Reconciliation of benefit obligation				
Obligation, beginning of year	$ 79,049	$ 74,179	$ 15,065	$ 14,269
Service cost	2,959	2,366	442	484
Interest cost	5,595	5,031	954	979
Plan amendments	1,716	--	--	--
Actuarial (gain) loss	9,443	(321)	54	249
Benefit payments	(3,621)	(2,206)	(892)	(916)
Obligation, end of year	$ 95,141	$ 79,049	$ 15,623	$ 15,065
Reconciliation of fair value of plan assets				
Fair value, beginning of year	$ 89,460	$ 76,894	$ --	$ --
Actual return on assets	15,855	14,557	--	--
Employer contribution	1,412	215	892	916
Benefit payments	(3,621)	(2,206)	(892)	(916)
Fair value, end of year	$103,106	$ 89,460	$ --	$ --
Funded status				
Funded status over (under), end of year	$ 7,965	$ 10,411	$(15,623)	$(15,065)
Unrecognized transition (asset) obligation	(74)	(60)	--	--
Unrecognized prior service cost	2,184	698	--	--
Unrecognized (gain) loss	(20,036)	(24,825)	680	353
Net	$ (9,961)	$(13,776)	$(14,943)	$(14,712)

The following table provides the amounts included in the Statement of Financial Position as of December 25, 1998, and December 26, 1997.

	Pension Benefits		Other Benefits	
(In thousands)	1998	1997	1998	1997
Accrued benefit liability	$ (10,272)	$(14,087)	$ (14,943)	$ (14,712)
Intangible asset	311	311	--	--
Net	$ (9,961)	$(13,776)	$ (14,943)	$ (14,712)

The components of net periodic benefit cost for the plans for 1998, 1997 and 1996 were as follows:

(In thousands)	Pension Benefits 1998	1997	1996	Other Benefits 1998	1997	1996
Service cost - benefits earned during the period	$ 2,959	$ 2,366	$ 2,366	$ 442	$ 484	$ 457
Interest cost on projected benefit obligation	5,595	5,031	4,699	954	979	924
Expected return on assets	(9,711)	(8,342)	(5,699)	--	--	--
Amortization of transition (asset) obligation	(3)	68	72	--	--	--
Amortization of prior service cost	230	95	95	--	--	--
Amortization of net (gain) loss	(1,067)	(944)	(442)	--	--	--
Cost of pension plans which are not significant and have not adopted SFAS No. 87	371	233	171	N/A	N/A	N/A
Net periodic benefit (credit) cost	(1,626)	(1,493)	1,262	1,396	1,463	1,381
Curtailment gain	(239)	--	--	--	--	--
Settlement gain	(271)	--	--	--	--	--
Net periodic benefit (credit) cost after curtailments and settlements	$ (2,136)	$(1,493)	$ 1,262	$1,396	$1,463	$1,381

The Company's retirement medical plan limits the annual cost increase that will be paid by the Company. In measuring the Accumulated Postretirement Benefit Obligation (APBO), a 6 percent maximum annual trend rate for healthcare costs was assumed for the year ending December 25, 1998. This rate is assumed to remain constant through the year 2001, decline to 5.5 percent in 2002 and 4.5 percent 2003, and remain at that level thereafter. The other assumptions used in the measurement of the Company's benefit obligation are shown below:

Weighted average assumptions	Pension Benefits 1998	1997	1996	Other Benefits 1998	1997	1996
Discount rate	6.5%	7.0%	7.0%	7.0%	7.0%	7.0%
Expected return on assets	11.0%	11.0%	9.0%	N/A	N/A	N/A
Rate of compensation increase	3.3%	3.3%	3.3%	N/A	N/A	N/A

At December 25, 1998, a 1 percent change in assumed healthcare cost trend rates would have the following effects:

	1% Increase	% Decrease
Effect on total of service and interest cost components of net periodic postretirement healthcare benefit cost	$ 235	$ (189)
Effect on the healthcare component of the accumulated postretirement benefit obligation	$2,343	$(1,918)

J. Earnings per Share

Earnings per share for all years presented has been calculated to reflect the three-for-two stock split declared on December 12, 1997. The following table sets forth the computation of basic and diluted earnings per share:

(In thousands, except per share amounts)	1998	1997	1996
Numerator:			
Net earnings available to common shareholders	$47,263	$44,716	$36,169
Denominators:			
Denominator for basic earnings per share - weighted average shares	22,941	25,575	25,908
Dilutive effect of stock options computed based on the treasury stock method using the average market price	606	591	394
Denominator for diluted earnings per share	23,547	26,166	26,302
Basic earnings per share	$ 2.06	$ 1.75	$ 1.40
Diluted earnings per share	$ 2.01	$ 1.71	$ 1.38

Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure

None.

PART III

Item 10. Directors and Executive Officers of the Registrant

The information under the heading "Executive Officers of the Company" in Part I of this 1998 Annual Report on Form 10-K and the information under the headings "Election of Directors, Nominees and Other Directors" on pages 2 through 4 and under the heading "Section 16(a) Beneficial Ownership Reporting Compliance" on page 13, of the Company's Proxy Statement for its 1999 Annual Meeting of Shareholders, to be held on May 4, 1999 (the "Proxy Statement"), is incorporated herein by reference.

Item 11. Executive Compensation

The information contained under the heading "Executive Compensation" on pages 5 through 11 of the Proxy Statement is incorporated herein by reference, other than the subsection thereunder entitled "Report of the Management Organization and Compensation Committee" and "Comparative Stock Performance Graph".

Item 12. Security Ownership of Certain Beneficial Owners and Management

The information contained under the heading "Beneficial Ownership of Shares" on pages 11 through 13 of the Proxy Statement is incorporated herein by reference.

Item 13. Certain Relationships and Related Transactions

The information under the heading "Certain Business Relationships" on page 11 of the Company's Proxy Statement for its 1999 Annual Meeting of Shareholders, to be held on May 4, 1999 (the "Proxy Statement"), is incorporated herein by reference.

PART IV

Item 14. Exhibits, Financial Statement Schedule, and Reports on Form 8-K

(a) The following documents are filed as part of this report:

(1) Financial Statements
See Part II

(2) Financial Statement Schedule — Page

All other schedules are omitted because they are not applicable, or not required, or because the required information is included in the Consolidated Financial Statements or Notes thereto.

(3) Management Contract, Compensatory Plan or Arrangement. (See Exhibit Index) 32
Those entries marked by an asterisk are Management Contracts, Compensatory Plans or Arrangements.

(b) Reports on Form 8-K
There were no reports on Form 8-K for the thirteen weeks ended December 25, 1998.

(c) Exhibit Index 32

Schedule II - Valuation and Qualifying Accounts
GRACO Inc. & Subsidiaries

(In thousands)

Description	Balance at beginning of year	Additions charged to costs and expenses	Deductions from reserves	Balance at end of year
Year ended December 25, 1998:				
Allowance for doubtful accounts	$ 2,200	$ 900	$ 500	$ 2,600
Allowance for obsolete and overstock inventory	4,700	2,900	3,300	4,300
Allowance for returns and credits	1,900	3,400	3,500	1,800
	$ 8,800	$7,200	$ 7,300	$ 8,700
Year ended December 26, 1997:				
Allowance for doubtful accounts	$ 2,400	$ 500	$ 700	$ 2,200
Allowance for obsolete and overstock inventory	5,100	1,500	1,900	4,700
Allowance for returns and credits	2,300	3,700	4,100	1,900
Valuation allowance for tax benefits	1,995	--	1,995	--
	$11,795	$5,700	$ 8,695	$ 8,800
Year ended December 27, 1996:				
Allowance for doubtful accounts	$ 2,800	$ 900	$ 1,300	$ 2,400
Allowance for obsolete and overstock inventory	5,900	2,500	3,300	5,100
Allowance for returns and credits	2,000	4,100	3,800	2,300
Valuation allowance for tax benefits	5,020	--	3,025	1,995
	$15,720	$7,500	$11,425	$11,795

1 Accounts determined to be uncollectible and charged against reserve, net of collections on accounts previously charged against reserves.

2 Items scrapped or otherwise disposed of during the year.

3 Credits issued and returns processed.

Signatures

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Graco Inc.

/s/James A. Earnshaw — March 18, 1999

James A. Earnshaw
President, Chief Executive Officer and Director

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

/s/James A. Earnshaw — March 18, 1999

James A. Earnshaw
President, Chief Executive Officer and Director
(Principal Executive Officer)

/s/Mark W. Sheahan — March 18, 1999

Mark W. Sheahan
Vice President and Treasurer
(Principal Financial Officer)

/s/James A. Graner — March 18, 1999

James A. Graner
Vice President and Controller
(Principal Accounting Officer)

D. A. Koch	Director, Chairman of the Board
G. Aristides	Director, and Vice Chairman
R. O. Baukol	Director
R. D. McFarland	Director
L. R. Mitau	Director
M. A. M. Morfitt	Director
D. R. Olseth	Director
J. L. Scott	Director
W. G. Van Dyke	Director

George Aristides, by signing his name hereto, does hereby sign this document on behalf of himself and each of the above named directors of the Registrant pursuant to powers of attorney duly executed by such persons.

/s/George Aristides — March 18, 1999

George Aristides
(For himself and as attorney-in-fact)

Exhibit Index

Exhibit Number	Description
3.1	Restated Articles of Incorporation as amended December 12, 1997. See also Exhibit 4.3. (Incorporated by reference to Exhibit 3.1 to the Compan's 1997 Annual Report on Form 10-K.)
3.2	Restated Bylaws. (Incorporated by reference to Exhibit 3 to the Company's Report on Form 10-Q for the twenty-six weeks ended June 27, 1997.)
4.1	Credit Agreement dated October 1, 1990, between the Company and First Bank National Association. (Incorporated by reference to Exhibit 5 to the Company's Report on Form 10-Q for the thirty-nine weeks ended September 28, 1990.)
4.2	Amendment 1 dated June 12, 1992, to Credit Agreement dated October 1, 1990, between the Company and First Bank National Association; and Amendment 2 dated December 31, 1992, to the same Agreement. (Incorporated by reference to Exhibit 1 to the Company's Report on Form 8-K dated March 11, 1993.) Amendment 3 dated November 8, 1993, and Amendment 4, dated February 8, 1994. (Incorporated by reference to Exhibit 4.2 to the Company's 1993 Annual Report on Form 10-K.) Amendment 5, dated April 10, 1995. (Incorporated by reference to Exhibit 4.2 to the Company's 1995 Annual Report on Form 10-K.) Amendment 6, dated September 27, 1996. (Incorporated by reference to Exhibit 4 to the Company's Report on Form 10-Q for the thirty-nine weeks ended September 27, 1996.) Amendment 7 dated May 27, 1997. (Incorporated by reference to Exhibit 4 to the Company's Report on Form 10-Q for the twenty-six weeks ended June 27, 1997.) Amendment 8, dated May 28, 1998. (Incorporated by reference to Exhibit 4 to the Company's Report on Form 10-Q for the twenty-six weeks ended June 26, 1998.)
4.3	Rights Agreement dated as of March 9, 1990, between the Company and Norwest Bank Minnesota, National Association, as Rights Agent, including as Exhibit A the form of the Certificate of Designation, Preferences and Rights of Series A Junior Participating Preferred Shares. (Incorporated by reference to Exhibit 1 to the Company's Report on Form 8-K dated March 19, 1990.)
4.4	Credit Agreement dated July 2, 1998, between the Company and U.S. Bank National Association. (Incorporated by reference to Exhibit 4 to the Company's Report on Form 10-Q for the thirty-nine weeks ended September 25, 1998.)
*10.1	1998 Corporate and Business Unit Annual Bonus Plan. (Incorporated by reference to Exhibit 10 to the Company's Report on Form 10-Q for the thirteen weeks ended March 27, 1998.)
*10.2	Deferred Compensation Plan Restated, effective December 1, 1992. (Incorporated by reference to Exhibit 2 to the Company's Report on Form 8-K dated March 11, 1993.) Amendment 1 dated September 1, 1996. (Incorporated by reference to the Company's Report on Form 10-Q for the twenty-six weeks ended June 27, 1997.)
*10.3	Executive Deferred Compensation Agreement. Form of supplementary agreement entered into by the Company which provides a retirement benefit to selected executive officers, as amended by Amendment 1, effective September 1, 1990. (Incorporated by reference to Exhibit 3 to the Company's Report on Form 8-K dated March 11, 1993.)
*10.4	Chairman's Award Plan. (Incorporated by reference to Exhibit 3 to the Company's Report on Form 8-K dated March 7, 1988.)
*10.5	Long Term Stock Incentive Plan, as amended December 12, 1997. (Incorporated by reference to Exhibit 10.5 to the Company's 1997 Annual Report on Form 10-K.)
*10.6	Retirement Plan for Non-Employee Directors. (Incorporated by reference to Attachment C to Item 5 to the Company's Report on Form 10-Q for the thirteen weeks ended March 29, 1991.)
*10.7	Deferred Compensation Plan for Non-Employee Directors. (Incorporated by reference to Exhibit 2 to the Company's Report on Form 8-K dated March 7, 1988.)
*10.8	Restoration Plan 1998 restatement. (Incorporated by reference to Exhibit 10.8 to the Company's 1997 Annual Report on Form 10-K.)

*10.9 Nonemployee Director Stock Plan, as amended November 6, 1997. (Incorporated by reference to Exhibit 10.11 to the Company's 1997 Annual Report on Form 10-K.)

*10.10 Stock Option Agreement. Form of agreement used for award of non-incentive stock options to executive officers, dated May 2, 1994. (Incorporated by reference to Exhibit 10.3 to the Company's Report on Form 10-Q for the twenty-six weeks ended July 1, 1994.)

*10.11 Stock Option Agreement. Form of agreement used for award of non-incentive stock options to selected officers, dated December 15, 1994, December 27, 1994 and February 23, 1995. (Incorporated by reference to Exhibit 10.16 to the Company's 1994 Annual Report on Form 10-K.)

*10.12 Stock Option Agreement. Form of agreement used for award of non-incentive stock options to executive officers, dated March 1, 1995. (Incorporated by reference to Exhibit 10 to the Company's Report on Form 10-Q for the thirteen weeks ended March 31, 1995.)

*10.13 Stock Option Agreement. Form of agreement used for award of non-incentive stock option to one executive officer, dated December 15, 1995. (Incorporated by reference to Exhibit 10.18 to the Company's 1995 Annual Report on Form 10-K.)

*10.14 Stock Option Agreement. Form of agreement used for award of non-incentive stock options to executive officers, dated March 1, 1996. (Incorporated by reference to Exhibit 10.19 to the Company's 1995 Annual Report on Form 10-K.)

*10.15 Form of salary protection arrangement between the Company and executive officers. (Incorporated by reference to Exhibit 10.21 to the Company's 1995 Annual Report on Form 10-K.)

*10.16 Nonemployee Director Stock Option Plan, as amended November 6, 1997. (Incorporated by reference to Exhibit 10.18 to the Company's 1997 Annual Report on Form 10-K.)

*10.17 Stock Option Agreement. Form of agreement used for award of nonstatutory stock options to nonemployee directors, dated May 7, 1996. (Incorporated by reference to Exhibit 10.4 to the Company's Report on Form 10-Q for the twenty-six weeks ended June 28, 1996.)

*10.18 Stock Option Agreement. Form of agreement used for award of non-incentive stock options to executive officers, dated February 28, 1997. (Incorporated by reference to Exhibit 10.24 to the Company's 1996 Annual Report on Form 10-K.)

*10.19 Stock Option Agreement Amendment. Form of amendment, dated March 8, 1997, used to remove alternative stock appreciation right from incentive stock option agreement dated February 25, 1993, for selected officers. (Incorporated by reference to Exhibit 10.25 to the Company's 1996 Annual Report on Form 10-K.)

*10.20 Stock Option Agreement Amendment. Form of amendment, dated March 8, 1997, used to remove alternative stock appreciation right from non-incentive stock option agreement dated May 4, 1993, for selected officers. (Incorporated by reference to Exhibit 10.26 to the Company's 1996 Annual Report on Form 10-K.)

*10.21 Key Employee Agreement. Form of agreement with officers and other key employees relating to change of control, dated April 2, 1997. (Incorporated by reference to Exhibit 10.1 to the Company's Report on Form 10-Q for the twenty-six weeks ended June 27, 1997.)

*10.22 Stock Option Agreement Amendment. Form of amendment, dated April 14, 1997, used to add change of control provision to non-incentive stock options to executive officer dated May 2, 1994, March 1, 1995 and March 1, 1996. (Incorporated by reference to Exhibit 10.6 to the Company's Report on Form 10-Q for the twenty-six weeks ended June 27, 1997.)

*10.23 Stock Option Agreement Amendment. Form of amendment, dated April 14, 1997, used to add change of control provision to non-incentive stock options to selected officers dated December 15, 1994. (Incorporated by reference to Exhibit 10.7 to the Company's Report on Form 10-Q for the twenty-six weeks ended June 27, 1997.)

*10.24 Stock Option Agreement Amendment. Form of amendment, dated April 14, 1997, used to add change of control provision to non-incentive stock options to one executive officer dated December 15, 1995. (Incorporated by reference to Exhibit 10.8 to the Company's Report on Form 10-Q for the twenty-six weeks ended

June 27, 1997.)

*10.25 Stock Option Agreement. Form of agreement used for award of non-incentive stock option to one executive officer, dated April 23, 1997. (Incorporated by reference to Exhibit 10.9 to the Company's Report on Form 10-Q for the twenty-six weeks ended June 27, 1997.)

*10.26 Stock Option Agreement. Form of agreement used for award of nonstatutory stock options to nonemployee directors, dated May 6, 1997. (Incorporated by reference to Exhibit 10.10 to the Company's Report on Form 10-Q for the twenty-six weeks ended June 27, 1997.)

*10.27 Executive Long Term Incentive Agreement. Form of restricted stock award agreement used for award to one executive officer, dated May 6, 1997. (Incorporated by reference to Exhibit 10.11 to the Company's Report on Form 10-Q for the twenty-six weeks ended June 27, 1997.)

*10.28 Stock Option Agreement. Form of agreement used for award of non-incentive stock option to two executive officers, dated May 6, 1997. (Incorporated by reference to Exhibit 10.12 to the Company's Report on Form 10-Q for the twenty-six weeks ended June 27, 1997.)

*10.29 Stock Option Agreement. Form of agreement used for award of nonstatutory stock options to nonemployee director, dated September 5, 1997. (Incorporated by reference to Exhibit 10.1 to the Company's Report on Form 10-Q for the thirty-nine weeks ended September 26, 1997.)

*10.30 Trust Agreement dated September 30, 1997, between the Company and Norwest Bank Minnesota, N.A. (Incorporated by reference to Exhibit 10.2 to the Company's Report on Form 10-Q for the thirty-nine weeks ended September 26, 1997.)

*10.31 Key Employee Agreement Amendment. Form of amendment dated January 9, 1998, revising payment reduction provisions. (Incorporated by reference to Exhibit 10.33 to the Company's 1997 Annual Report on Form 10-K.)

*10.32 Stock Option Agreement. Form of agreement used for award of non-incentive stock options to executive officers, dated February 28, 1998. (Incorporated by reference to Exhibit 10.1 to the Company's Report on Form 10-Q for the thirteen weeks ended March 27, 1998.)

*10.33 Separation and Release Agreement between Charles M. Osborne and the Company, dated May 29, 1998.

*10.34 Employment Agreement between the Company and executive officer dated December 22, 1998.

11 Statement of Computation of Earnings per share included in Note J on page 28.

21 Subsidiaries of the Registrant included herein on page 36.

23 Independent Auditors' Consent included herein on page 36.

24 Power of Attorney included herein on page 37.

27 Financial Data Schedule (EDGAR filing only.)

99 Cautionary Statement Regarding Forward-Looking Statements.

*Management Contracts, Compensatory Plans or Arrangements.

Pursuant to Item 601(b)(4)(iii) of Regulation S-K, copies of certain instruments defining the rights of holders of certain long-term debt of the Company and its subsidiaries are not filed as exhibits because the amount of debt authorized under any such instrument does not exceed 10 percent of the total assets of the Company and its subsidiaries. The Company agrees to furnish copies thereof to the Securities and Exchange Commission upon request.

Exhibit 21

Subsidiaries of Graco Inc.

The following are subsidiaries of the Company:

Subsidiary	Jurisdiction of Organization	Percentage of Voting Securities Owned by the Company
Equipos Graco Argentina S.A.	Argentina	100%*
Graco Barbados FSC Limited	Barbados	100%
Graco Canada Incorporated	Canada	100%
Graco Chile Limitada	Chile	100%*
Graco do Brasil Limitada	Brazil	100%*
Graco Europe N.V.	Belgium	100%*
Graco GmbH	Germany	100%
Graco Hong Kong Limited	Hong Kong	100%*
Graco K.K.	Japan	100%
Graco Korea Inc.	Korea	100%
Graco Limited	England	100%*
Graco N.V.	Belgium	100%*
Graco S.A.	France	100%*
Graco S.r.l.	Italy	100%*

* Includes shares held by selected directors and/or executive officers of the Company or the relevant subsidiary to satisfy the requirements of local law.

Exhibit 23

Independent Auditors' Consent

We consent to the incorporation by reference in Registration Statement No. 333-17691 on Form S-8 (the Company's Long- Term Stock Incentive Plan), in Registration Statement No. 333-17787 on Form S-8 (the Company's Employee Stock Purchase Plan), in Registration Statement No. 33-54205 on Form S-8 (the Company's Nonemployee Director Stock Plan) and in Registration Statement No. 333-03459 on Form S-8 (the Company's Nonemployee Director Stock Option Plan) of our report dated January 18, 1999, appearing in this Annual Report on Form 10-K of Graco Inc. for the year ended December 25, 1998.

/s/Deloitte & Touche LLP
Deloitte & Touche LLP
Minneapolis, Minnesota
March 23, 1999

Exhibit 24

Power of Attorney

Know all by these presents, that each person whose signature appears below hereby constitutes and appoints George Aristides or Mark W. Sheahan, that person's true and lawful attorney-in-fact and agent, with full power of substitution and resubstitution for that person and in that person's name, place and stead, in any and all capacities, to sign the Report on Form 10-K for the year ended December 25, 1998, of Graco Inc. (and any and all amendments thereto) and to file the same with the Securities and Exchange Commission, granting unto said attorney-in-fact and agent, full power and authority to do and perform each and every act and thing requisite or necessary to be done in and about the premises, as fully to all intents and purposes as that person might or could do in person, hereby ratifying and confirming all that said attorney-in-fact and agent, or his substitutes, may lawfully do or cause to be done by virtue hereof.

In witness whereof, this Power of Attorney has been signed by the following persons on the date indicated.

	Date
/s/G. Aristides G. Aristides	February 19, 1999
/s/R. O. Baukol R. O. Baukol	February 19, 1999
/s/D. A. Koch D. A. Koch	February 19, 1999
/s/R. D. McFarland R. D. McFarland	February 19, 1999
/s/L. R. Mitau L. R. Mitau	February 19, 1999
/s/M. A.M. Morfitt M. A.M. Morfitt	February 19, 1999
/s/D. R. Olseth D. R. Olseth	February 19, 1999
/s/J. L. Scott J. L. Scott	February 19, 1999
/s/W. G. Van Dyke W. G. Van Dyke	February 19, 1999

Exhibit 10.33

SEPARATION AND RELEASE AGREEMENT

THIS AGREEMENT is effective the 29th day of May, 1998, by and between Graco Inc., a Minnesota corporation ("Graco"), with its principal offices at 4050 Olson Memorial Highway, Golden Valley, Minnesota 55422 and Charles M. Osborne, an individual, residing at One Red Pine Road, North Oaks, Minnesota 55127 ("Mr. Osborne").

WHEREAS, Mr. Osborne is now employed by Graco; and

WHEREAS, The parties have agreed that Mr. Osborne will resign as an officer and employee of Graco effective May 31, 1998, and will terminate his employment relationship with Graco in accordance with the terms of this Agreement.

NOW, THEREFORE, It is hereby mutually agreed by and between the parties for good and valuable consideration as follows:

1. Separation Payment

On or before June 5, 1998, Graco will pay to Mr. Osborne in a lump sum as a separation payment the amount of three hundred fifty thousand dollars ($350,000) dollars, subject to tax withholding and deductions required by law. This payment is made in lieu of any other payment of salary, severance, bonus, or other compensatory amount to which Mr. Osborne is or may be entitled.

2. Annual Bonus Plan

Mr. Osborne shall not be entitled to any payment under the 1998 Corporate and Business Unit Annual Bonus Plan.

3. Benefits

Mr. Osborne's entitlement to, continuation or cessation of employee benefits following the termination of his employment is described in a letter from the Graco Benefits Department to Mr. Osborne's attention, attached hereto as Exhibit A and incorporated herein by reference.

4. Cooperation

Mr. Osborne shall render all reasonable cooperation to Graco in connection with the prosecution or defense of any lawsuit or other judicial or administrative action, including participating as a source of information or witness in any such action. Graco shall reimburse Mr. Osborne for any reasonable out-of-pocket expenses (including attorneys' fees, if necessary) incurred by him in connection with rendering such cooperation.

5. Confidentiality

a. Mr. Osborne hereby agrees that, for a period of three (3) years after May 31, 1998, he will not, directly or indirectly, disclose any Confidential Information, as defined in subsection (b) below, to any other party, and will not in any way use such Confidential Information in the course of his employment.

b. As used herein, the term "Confidential Information" shall mean all information which is treated as confidential or proprietary by Graco in the normal course of its business, including, without limitation, documents so marked, or is a trade secret of Graco, which has been disclosed by Graco to Mr. Osborne including, without limitation, information relating to Graco products, processes, product development or research, equipment, machinery, apparatus, business operations, financial results or condition, strategic plans or projections, customers, suppliers, marketing, sales, management practices, technical information, drawings, specifications, material, and the like, and any knowledge or information developed by Mr. Osborne relating to the same, provided, however, that Confidential Information shall not include information which is at the time of disclosure, or thereafter becomes, a part of the public domain through no act or omission by Mr. Osborne or information which Mr. Osborne is required to disclose in a court or other judicial proceeding or is otherwise legally required to disclose.

c. The provisions of this Section 5 are in addition to, and not in lieu of, the fiduciary and other duties and obligations of Mr. Osborne as an employee, officer and director of Graco, and this Section 5 does not limit said obligations in any way, by time or otherwise.

6. Release

a. Except with respect to the provisions of this Agreement and the provisions of the letter from the Benefits Department, attached hereto as Exhibit A, Mr. Osborne hereby releases and forever discharges Graco and its officers, employees, agents, successors, and assigns from any and all claims, causes of action, demands, damages, liability and responsibility whatsoever, arising prior to the date of this Agreement, including without limitation, any rights or claims for further compensation, or any rights to participate in any Company-sponsored program relating to the purchase or acquisition of any Graco common stock, preferred stock, or other equity in Graco or any subsidiary thereof, except as specifically provided in this Agreement, including the Exhibit hereto, or any right or claim Mr. Osborne may have or assert under the common law or any state, municipal, federal, or other statute or regulation regarding the rights of employees generally or based on discrimination on the basis of race, creed, gender, age, or other protected status. This Section 6 shall not affect Mr. Osborne's rights to indemnification as an officer, director, and employee of Graco under Graco's by-laws and applicable Minnesota law nor any rights which he has accrued by participating in any Graco benefit plan, subject to the provisions of this Agreement and the terms and conditions set forth in such plan as of his resignation date.

b. Mr. Osborne certifies, represents and agrees that:

(i) this Agreement is written in a manner that he understands;

(ii) he understands that this Section 6 specifically waives any rights or claims he may have arising under federal, state, and local laws prohibiting employment discrimination, such as the Age Discrimination in Employment Act, the Minnesota Human Rights Act, Title VII of the Civil Rights Act of 1964, the Rehabilitation Act of 1973, the Americans with Disabilities Act and/or any claims for damages or for injuries based on common law theories of contract, quasi-contract or tort;

(iii) the waiver herein of rights or claims are to those which may have arisen prior to the execution date of this Agreement;

(iv) a portion of the consideration set out in this Agreement is in addition to compensation that he may already have been entitled to;

(v) he has been specifically advised in writing to consult with an attorney prior to executing this Agreement;

(vi) he has been informed that he has a period of at least twenty-one (21) calendar days within which to consider this Agreement;

(vii) he specifically understands that he may revoke this Agreement for a period of at least fifteen (15) calendar days following his execution of this Agreement, and that this Agreement is not effective or enforceable until the fifteen (15) day revocation period has expired;

(viii) if he decides to revoke this Agreement within said fifteen (15) day period, he should provide written notice to the Vice President, General Counsel and Secretary, delivered in person or by mail. If his revocation is sent by mail, it must be postmarked on or before June 15, 1998, properly addressed to Robert M. Mattison, Vice President, General Counsel and Secretary, Graco Inc., P.O. Box 1441, Minneapolis, MN. 55440, and sent by certified mail, return receipt requested. Mr. Osborne understands that Graco will have no obligation to pay him anything under this Agreement if he revokes his acceptance within the time limit specified, and that he will be obligated to immediately refund to Graco all sums paid to him by Graco pursuant hereto.

(ix) Mr. Osborne expressly agrees that the waiver of his rights pursuant to the Agreement is knowing and voluntary on his part.

7. Continuation as Director

As of June 1, 1998, Mr. Osborne shall be compensated for his services as a member of the board of directors in accordance with the compensation practice of Graco for non-employee directors. All stock option grants made to Mr. Osborne solely because of his position as a member of the board of directors prior to him becoming an employee of Graco shall not be affected in any way by this Agreement.

8. Applicable Law

Except to the extent governed by federal law, this Agreement and any controversies between the parties shall be governed by and construed in accordance with the laws of the State of Minnesota.

9. Entire Agreement

This Agreement, including Exhibit A hereto, constitutes the entire agreement and understanding between the parties with respect to the subject matter hereof, and, except as otherwise specifically provided herein or in Exhibit A, specifically supersedes and replaces any and all prior written or oral agreements or understandings. This Agreement may not be amended except in a writing signed by authorized representatives of both parties.

10. Headings

The headings of the paragraphs herein are included solely for the convenience of reference and shall not control the meaning or interpretation of any provisions of this Agreement.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement in duplicate originals on the day and year first above written.

GRACO INC.

/s/George Aristides
- -------------------
George Aristides
Chief Executive Officer

CHARLES M. OSBORNE

/s/Charles M. Osborne

Exhibit A

May 7, 1998

Mr. Charles Osborne
1 Red Pine Road
North Oaks, MN 55127

Dear Chuck:

This letter will review the status of your Graco benefit programs following your termination of employment with the Company, and advise you of decisions that need to be made concerning these programs. In summarizing the benefits in this letter, May 30, 1998 was used as your last day of employment.

Health Coverage

Your group Health Care coverage through Medica would normally end May 31, 1998. However, you do have the option to retain family coverage until you are eligible for coverage through a new employer or for a period of 18 months, whichever is shorter. Coverage can be extended from June, 1998 through November, 1999. You may choose to continue coverage for three months at the employee premium rate of $67.44 per month. You may then continue coverage for an additional 15 months by paying the full $458.51 monthly premium. Premium rates and benefit levels are subject to future changes.

To continue your Health Care coverage, it will be your responsibility to pay the monthly premium to Graco. We in turn will transmit payment to the health care provider. Your check or money order should be made payable to Graco Inc., and sent to the Payroll Department by the first day of each month. To guarantee uninterrupted medical coverage, the first payment should be submitted on or before June 15, 1998. However, you do have until July 30, 1998, to request reinstatement of your coverage. Along with your request, you will need to submit retroactive premium payments back to the time your coverage as an employee ceased. Also, any medical expenses you incur for this period of retroactive coverage, will be delayed in processing until your coverage is reinstated. Failure to make timely payment will result in the automatic termination of coverage. There are no statements or reminders sent out. Please indicate on the enclosed form whether you wish to continue your Health coverage. Please note the following attachment on 1996 changes to continuation coverage rules applicable to group health plans under the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA), as amended.

Dental Coverage

Your Dental coverage through Prudential would normally end May 31, 1998. However, you do have the option to retain family coverage until you are eligible for coverage through a new employer or for a period of 18 months, whichever is shorter. Your coverage can be extended from June, 1998 through November, 1999, by paying the full $59.65 monthly premium. Premium rates and benefit levels are subject to future changes. Payment is handled in the same manner as for Health Care. Please indicate on the enclosed form whether you wish to continue your Dental coverage.

Executive Disability Benefit

Your Long Term Disability coverage will continue through May 31, 1998. At that time, the $12,167 group LTD coverage will terminate, but you hve the option to continue the $4,000 individual policy if you are interested. We will have the agent, Mr. Bob Westenberg, contact you to discuss the program.

Life Coverage

Your Executive Basic and Supplemental Life coverage would normally terminate on May 31, 1998. You have the option of extending your $200,000 Executive Basic Life coverage as well as your $400,000 Supplemental Life coverage until you are eligible for coverage through a new employer, or for a period of 18 months, whichever is shorter. Coverage can be extended from June, 1998 through November, 1999, by paying the following monthly premium:

o	Basic Life Coverage	$ 54.00
o	Supplemental Life Coverage	144.00

	Total	198.00 Per Month
		=======

Premium rates are subject to future changes. Payment is handled in the same manner as Health coverage. Please indicate on the enclosed form whether you wish to continue your Life coverage through our 18 month extension.

Conversion to a private policy is available either when your coverage as an employee ends or after you complete the full 18 month extension. You may convert any increment of $1,000 from a minimum of $5,000 up to a maximum of your total coverage through Graco. If you convert now, conversion is to a whole life policy with the rate set for the life of the policy. Payments can be established on a quarterly, semi-annual or annual basis. If you convert after your 18 month extension, conversion is to a three year renewable term policy. This means that every three years your premium will be adjusted to reflect your new age. Premiums are paid on an annual basis only. If you wish to convert to a private policy, it is your responsibility to contact us for a conversion form. You have 31 days from the date your coverage would normally end to make this conversion.

Personal Accident Coverage

Your $250,000 24-Hour Personal Accident Insurance benefit would normally terminate on May 31, 1998. You have the option of converting your family coverage to an individual policy by making written application to our insurance carrier within 30 days of your coverage termination date. If you are interested in converting your coverage, simply indicate by checking the box on the enclosed form.

Expense Reimbursement Account

You are currently enrolled in Graco's healthcare expense reimbursement account. Claims on expenses incurred prior to leaving Graco may be filed between now and calendar year-end. To receive reimbursement on expenses incurred after leaving Graco, you will be required to submit ongoing monthly after-tax contributions between now and the end of the year. A check made out to Graco in the amount of $200.00 should be sent to my attention by the first of each month. Please let me know if you wish to do this.

Graco Employee Investment Plan

You are eligible for a distribution from your Employee Investment Plan account. As of May 7, 1998, your account balances are as follows:

Pre-Tax Account	$13,839.62
Employer Account	6,925.38
Rollover Account	10,589.42

Total EIP Account	$31,354.42
	==========

You may elect one of the following distribution options:

- o Single lump sum.
- o Installment payments paid annually, quarterly, or monthly.
- o Defer distribution until the close of the calendar year in which you reach age 70 1/2. (Note: Maximum age to which distribution can be deferred. Distribution may be deferred to earlier date.)
- o Rollover of Pre-Tax and Employer contributions and investment earnings to Individual Retirement Account (IRA) or new employer plan. Rollover may be made directly to your IRA or new employer plan, without withholding taxes being applicable. Rollovers may be distributed to you for transmission to a new plan, but 20% withholding will apply.*

To receive a distribution of your Employee Investment Plan assets, please telephone the Benefits Advantage Hotline at (888) 319-9451. In Minneapolis/St. Paul, dial 316-1355. The Hotline will give you directions for accessing a total distribution in either a single lump sum cash amount or to be rolled over to another plan or qualified IRA. If you wish to collect installment payments, please contact me. If you decide to defer distribution of your account, you do not need to take any action at this time.

You have not paid taxes on any of these funds, and the entire account balance will be taxable to you when funds are distributed. You should note that the taxable portion of your account balance is subject to federal income tax. If you receive any payment before you reach age 59 1/2, an additional 10% income tax will apply to all taxable amounts. These include your Pre-Tax contributions, Employer contributions, your Profit Sharing Account (if you were employed with Graco prior to 1968) and earnings on all accounts.

*Note: You will want to review the enclosed information concerning a lump sum distribution from the Employee Investment Plan, and the procedure for direct or other rollover of your distribution to an IRA or other employer plan. Rules are detailed in the enclosure.

After you have contacted the Hotline and requested a complete withdrawal or rollover, you will receive a form in the mail from Norwest. This form should be completed by you and returned to Norwest no earlier than 30 days following your termination. An application received before that point in time cannot be processed by Norwest.

Graco Employee Stock Purchase Plan

Since only Graco employees can buy stock through the Employee Stock Purchase Plan at the end of the purchase period, you will receive a lump sum distribution of your account approximately 6-8 weeks after your employment termination date. The distribution will include all of your contributions to the Plan, as well as the 5.70% interest your money has earned, calculated on a simple interest basis.

Graco Employee Retirement Plan

The Employee Retirement Plan provides a vested benefit at retirement age for employees who have completed five years of service with the Company. Since your period of service with Graco was less than five years, you are not entitled to a retirement benefit.

Please complete and return the enclosed paperwork as soon as possible. If you have any questions concerning your benefits, please feel free to contact me at (612) 623-6630. I wish you the very best as you move on from Graco and explore other options that are available to you.

Sincerely,

Karen Chapin
Director of Benefits and Risk Management

CERTIFICATE OF GROUP HEALTH PLAN COVERAGE

* IMPORTANT - This certificate provides evidence of your prior health coverage. You may need to furnish this certificate if you become eligible under a group health plan that excludes coverage for certain medical conditions that you have before you enroll. This certificate may need to be provided if medical advice, diagnosis, care, or treatment was recommended or received for the condition within the 6-month period prior to your enrollment in the new plan. If you become covered under another group health plan, check with the plan administrator to see if you need to provide this certificate. You may also need this certificate to buy, for yourself or your family, an insurance policy that does not exclude for medical conditions that are present before you enroll.

1. Date of this certificate: May 7, 1998

2. Name of group health plan: Medica

3. Name of participant: Charles Osborne

4. Social Security Number of participant: ###-##-####

5. Name of any dependents to whom this certificate applies: Victoria Osborne, Marc Osborne, Maria Osborne, Catherine Osborne, Daniel Osborne, John Osborne

6. Name, address, and telephone number of plan administrator or Issuer responsible for providing this certificate:

   Graco, Inc.
   P.O. Box 1441
   Minneapolis, MN 55440

7. For further information, call: (612) 623-6628

8. If the individual(s) identified in line 3 and line 5 has at least 18 months of creditable coverage (disregarding periods of coverage before a 63-day break), check here and skip lines 9 and 10.

9. Date waiting period or affiliation period (if any) began: April 28, 1997

10. Date coverage began: May 1, 1997

11. Date coverage ended: May 31, 1998

Note: separate certificates will be furnished if information is not identical for the participant and each beneficiary.

December 22, 1998

Mr. James A. Earnshaw
6407 Oxbow Bend
Chanhassen, MN. 55317

Dear Jim:

On behalf of the Board of Directors, I am extremely pleased to extend to you the following offer to become the President and Chief Executive Officer of Graco Inc., as follows:

- Base salary: $30,000 per month. Compensation is reviewed annually by the Management Organization and Compensation Committee.

- Annual Bonus: Participation in the Annual Bonus Program, with a maximum payment for 1999 of 80% of base salary paid during the year.

- Stock Options: Under our Long Term Stock Incentive Plan, an initial grant of 50,000 shares, effective the first day of your employment, and a regular annual grant in 1999 of 40,000 shares, effective on the date those grants are made. Future grants are determined annually by the Management Organization and Compensation Committee. These are 10 year non-ISO options at the market price on the date of grant, with 25% vesting on the 2nd, 3rd, 4th and 5th anniversaries. As we discussed, these initial two grants will also provide for immediate vesting if you are involuntarily terminated for other than gross and willful misconduct during the first two years of employment, and be exercisable for 6 months after such termination.

- Severance Pay: In the event that your employment is terminated involuntarily during the first two years after your first date of employment for other than gross and willful misconduct, you will be paid an amount equal to two years of your then base salary. After said two years your severance pay will be in accordance with Graco's regular practice of one year of base salary. For purposes of this letter, gross and willful misconduct includes, but is not limited to, wrongful appropriation of Company funds, serious violation of Company policy or the commission of a felony.

- Key Employee Agreement: You will be extended a Key Employee Agreement, effective your first day of employment, which essentially provides for two years of base salary, expected bonus and benefits if you are terminated within two years after a change of control of the Company. Also, all stock options automatically fully vest upon a change of control.

- Benefits: Participation in Graco's comprehensive employee benefit plans.

- Club dues: Payment of your regular dues at the Minneapolis Club and the Lafayette Club.

As we discussed, we anticipate that you will start on March 1, 1999. You will immediately be elected to the Board of Directors. Until April 30, I will continue to run the day to day operations while you learn about the business. On May 1 you will be in charge.

To accept this offer, please sign the enclosed copy of this letter and return it to me. There are also some routine tests and checks that must be performed, and forms to complete, that are explained in the letter from Michael Galdonik you have received. He has also provided you with a description of our benefits package.

Jim, we are delighted at the prospect of you joining Graco. I know that with your experience and track record, you are the right person to lead the company to even greater success in the years to come.

Yours very truly,

/s/George Aristides
George Aristides
Chief Executive Officer

Agreed and Accepted:

/s/James A. Earnshaw
James A. Earnshaw

5

Financial Data Schedule for the Year Ended 12/25/98

0000042888
GRACO INC.
1,000
U.S. Dollars

12-MOS
DEC-25-1998
DEC-27-1997
DEC-25-1998
1
3,555
0
84,546
4,400
34,018
131,320
199,122
102,756
233,702
82,966
115,739
0
0
20,097
(10,784)
233,702
432,185
432,185
212,784
212,748
148,038
764
5,319
71,363
24,100
47,263
0
0
0
47,263
2.06
2.01

Exhibit 99

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

Graco Inc. (the "Company") wishes to take advantage of the "safe harbor" provisions regarding forward-looking statements of the Private Securities Litigation Reform Act of 1995 and is filing this Cautionary Statement in order to do so.

From time to time various forms filed by the Company with the Securities and Exchange Commission, including the Company's Form 10-K, Form 10-Q and Form 8-K, its Annual Report to Shareholders, and other written documents or oral statements released by the Company, may contain forward-looking statements. Forward-looking statements generally use words such as "expect," "foresee," "anticipate," "believe," "project," "should," "estimate," and similar expressions, and reflect the Company's expectations concerning the future. Such statements are based upon currently available information, but various risks and uncertainties may cause the Company's actual results to differ materially from those expressed in these statements. Among the factors which management believes could affect the Company's operating results are the following:

- With respect to the Company's business as a whole, the Company's prospects and operating results may be affected by:

    - changing economic conditions in the United States and other major world economies, including economic downturns or recessions and foreign currency exchange rate fluctuations;

    - international trade factors, including changes in international trade policy, such as trade sanctions, increased tariff barriers and other restrictions, weaker protection of the Company's proprietary technology in certain foreign countries, the burden of complying with foreign laws and standards, and potentially adverse taxes;

    - the ability of the Company to develop new products and technologies, maintain and enhance its market position relative to its competitors, maintain and enhance its distribution channels, realize productivity and product quality improvements, and continue to control expenses.

    - the ability of the Company and its suppliers, customers, creditors and financial service organizations to implement information processing software and hardware that will accommodate the Year 2000;

    - disruption in operations, transportation, communication, sources of supply, customer operations or payment, caused by political or economic instability, acts of God, labor disputes, war, embargo, fire or other cause beyond its reasonable control.

    - changes in the markets in which the Company participates, including consolidation of competitors and major customers.

- The prospects and operating results of the Company's Contractor Equipment Division may be affected by: variations in the level of residential, commercial and institutional building and remodeling activity; the availability and cost of financing; changes in the environmental regulation of coatings; consolidation in the paint equipment manufacturing industry; changes in construction materials and techniques; the cost of labor in foreign markets; the regional market strength of certain competitors; the level of government spending on infrastructure development, road construction and repair; and the nature and extent of highway safety regulation.

- The prospects and operating results of the Company's Industrial/Automotive Equipment Division may be affected by: the capital equipment spending levels of industrial customers; the availability and cost of customer financing; changes in the environmental regulation of coatings; changes in the technical characteristics of materials; changes in application technology; the ability of the Company to meet changing customer requirements; the equipment purchase plans of major automobile manufacturers worldwide (which are in turn impacted by the level of automotive sales worldwide); changes in automotive manufacturing processes; the pricing strategies of competitors; consolidation in the automobile manufacturing industry worldwide; and the success of the Company in moving its automotive customers from custom-designed systems purchased directly from the Company to the purchase of package modules sold through integrators and distributors.

- The prospects and operating results of the Company's Lubrication Equipment Division may be affected by consolidation in the oil industry, the development of extended life lubricants for vehicles, the reduction in the need for changing vehicle lubricants, and variations in the equipment spending levels of the major oil companies.