



Donaldson Company, Inc. 2015 SHAREHOLDERS' LETTER

DEAR SHAREHOLDERS,

In 2015, Donaldson joined a short list of publicly traded companies that are at least 100 years old, and I am honored to lead the Company as it begins the journey towards its bicentennial.

The aspects of our culture that carried us through our first 100 years remain relevant today:

- Donaldson is a technology-led filtration company;
- We are focused on adding value for our Customers with our unique filtration solutions, and
- Our global team is committed to delivering superior results for our Customers and Shareholders.

Integrity is one of Donaldson's core values, and central to who we are as a Company. While the recent revenue recognition issue in our European Gas Turbine business was disappointing, it is not a reflection on how we operate as a Company. Following the investigation, we are focused on reemphasizing our core values, enhancing our training and strengthening our control processes. I am confident in our ability to move past this situation and mitigate any risk of this happening again.



Donaldson's Mission and Values

Addressing the Environment

The year of our centennial was particularly challenging, as weakness in many of our end markets, global economic uncertainty, and dramatic changes in foreign exchange rates all contributed to results that were below our projections heading into the fiscal year.

Our FY15 sales were \$2.4 billion, which includes a negative impact from foreign currency translation of \$135 million. Excluding this impact, organic sales increased 1% above last year, reflecting our continued ability to outperform the markets we serve. FY15 adjusted earnings per share, which excludes restructuring and other one-time charges, were \$1.58.

From an operational perspective, we addressed last year's challenges by taking action.

Our Customers are always our top priority—especially as many of them faced much lower demand for their products due to end-market volatility. We continued to partner closely with them in the design and development of breakthrough new products using our latest technologies, while also ensuring they had the products they needed where and when they needed them.

Throughout the year, we continued investing in our key growth initiatives. For example, we grew our distribution footprint, with notable success in Latin America and Eastern Europe; we are accelerating liquid production in our new facility in Poland, and we continued the roll-out of our global ERP solution.

However, we also made the difficult decision to restructure parts of the Company, which aligned the cost and investment profile in those businesses with their current and projected market conditions. These actions are expected to deliver \$35 million of annual savings, providing us with the flexibility to both improve our profitability and returns while investing in our long-term growth opportunities.

I am proud of our ability to respond proactively to dramatic shifts in the business environment, which positions us very well for future growth.

Positioning for Growth

During FY15, we made significant progress on our key growth initiatives, including:

- Further expansion of our core businesses,
- Continued geographic expansion, and
- Disciplined execution of our acquisition strategy.

There were many new examples of success, with several of them supporting at least one of these growth initiatives.

Continued expansion of our leading filtration technologies squarely addresses our goal of expanding the core business. Winning new OEM Customer equipment platforms with these innovative products secures a high retention rate for future replacement filter sales for our OEM Customers and us.



The advanced technology and innovative design in PowerCore® meets Customer requirements in both diesel engines (left) and industrial applications (right).

The successive generations of PowerCore® technology serve as a significant example of our focus on product innovation. Last year, PowerCore sales grew 10% to \$186 million. In Engine Products, which represents about 90% of total PowerCore sales today, both first-fit and replacement filter sales growth was significantly better than the Company averages for each of those businesses.

PowerCore's tremendous success with our Customers has led to significantly increased demand for this type of breakthrough filtration solution. To further expand our offering, we developed PowerPleat™, a solution in Engine Air that can replace many legacy technologies. We are now in the early stages of introducing PowerPleat to our Customers, and we are excited about winning new platforms with this technology.

Liquid Filtration is one of our key strategic growth opportunities. With our advanced Synteq® XP media technology, we have already won a significant number of new OEM fuel filtration programs, and we have a full pipeline of additional opportunities.

We also invested in growth of our traditional aftermarket sales. In Latin America, for example, our new distribution capabilities in Peru, and the expansion of our parts offerings in our existing distribution centers in Mexico, Chile, and Brazil, resulted in a local-currency sales increase of 13%. We also opened a distribution center in Slovakia to further grow our Eastern European aftermarket businesses. Across the world, including North America, we focused on product availability and distribution reliability, further strengthening our position with our OEMs, distributors and dealers.

Within our Industrial business, our new dust collection product, Downflo® Evolution, or DFE, features a much smaller footprint and an innovative replacement filter that offers significantly faster maintenance. During its first year in the market, DFE orders grew to \$11 million, and we are now introducing this product line into Europe.

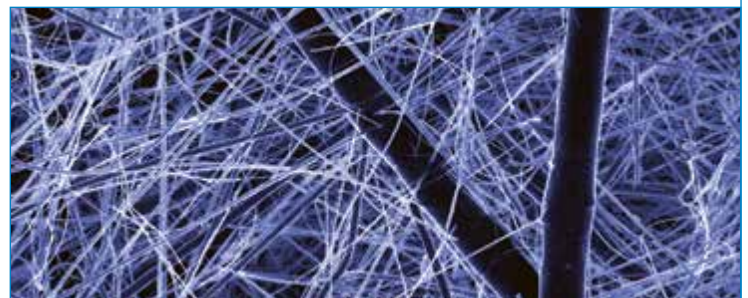
As a result of our redesigned M&A process, we announced four acquisitions in the past year, including:

- Northern Technical (located in Abu Dhabi), a manufacturer of filtration systems and replacement filters for gas turbines,
- IFIL USA, a manufacturer of replacement filters for our dust collection business,
- Engineered Products Company (located in the U.S.), manufacturer of the Filter Minder® brand of indicators and sensors for air filtration systems, and
- Industrias Partmo (located in Colombia), a distributor and manufacturer of air and liquid replacement filters (we anticipate closing the transaction during our fiscal second quarter).

Each of these acquisitions supports at least one of our organic growth initiatives, and the acquisitions we have closed are expected to add between \$15 million and \$20 million of additional sales in FY16.

Commitment to Shareholders

In FY15, we returned 167% of our net income to Shareholders through cash dividends and share repurchase. During the year, we paid dividends of \$91 million and repurchased 4.7% of our diluted outstanding shares.



The first air filters produced at our new plant in Skarbimierz, Poland. Later this fiscal year, we'll begin producing liquid filters at this facility.

Synteq® XP delivers best-in-class fuel filtration, which has become increasingly important with high-performing engines and the increased use of biodiesel fuel.



Our new dust collection product, Downflo® Evolution, leverages innovative design and faster maintenance to meet our Customers' needs.

We continue to expand our liquid filtration offering, with a particular focus on growing our fuel filter business by leveraging our technology.

Additionally, we retain an after-tax ROI target of 15%, and our capital deployment strategy remains focused on:

- Investments to support organic growth,
- Acquisitions that can accelerate our growth,
- Dividends, and
- Share repurchase.

Continuing to Focus on What We Can Control

Based on our expectation that there will not be an imminent recovery in end markets or the global economy, we are focusing on those aspects of our initiatives that are within our control. For example:

- We will continue to win new OEM first-fit programs as we expand our technology offerings and leverage our strong Customer relationships;
- Our proprietary systems utilizing innovative technologies already in production will grow our aftermarket replacement filter business;
- We will leverage the distribution and local production investments we have made across the globe, and
- We will continue to expand our product lines for our Customers.

Internally, we will complete the roll-out of our global ERP system. This tremendous achievement will mark the first time in our history when all of our operations around the world will be on one standard system. Being on one global system will improve and enhance our ability to support our Customers wherever they need us.

All of the work we have planned in FY16 will further strengthen our Company's foundation as we look toward FY17 and beyond.

Thank You

I want to thank all of my fellow Employees for your efforts. Each of you plays a key role in our success, and I am appreciative of your unwavering commitment to our Customers and Shareholders.

I thank our Customers for the continued opportunity to address your filtration needs. We are proud of the role we play in helping your equipment and products perform for your Customers, and we recognize the need to continue advancing our products to earn your business every day.

Finally, I thank you, our Shareholders, for your continued confidence and support, especially as we worked through the recent investigation into our European Gas Turbine business.

Sincerely,

Tod E. Carpenter
President and CEO



Safe Harbor Statement

The Company desires to take advantage of the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995 (the "Act") and is making this cautionary statement in connection with such safe harbor legislation. This document contains forward-looking statements, including, without limitation, forecasts, plans, trends, and projections relating to our business and financial performance and global economic conditions, which involve uncertainties that could materially impact results. All statements other than statements of historical fact are forward-looking statements, and these statements do not guarantee future performance. For a more detailed explanation of these risks and uncertainties, please see the Company's Form 10-K.

FIVE-YEAR COMPARISON OF RESULTS

(Dollars and shares outstanding are in millions, except per share amounts)

Twelve Months Ended July 31,

	2015	2014	2013	2012	2011
Operating Results					
Net Sales	\$2,371	\$2,473	\$2,437	\$2,493	\$2,294
Gross Margin Percentage	34.1%	35.5%	34.8%	35.0%	35.5%
Operating Income Percentage	12.2%	14.4%	14.1%	14.6%	13.7%
Net Earnings	\$208	\$260	\$247	\$264	\$225
Diluted Earnings per Share	\$1.49	\$1.76	\$1.64	\$1.73	\$1.43
Additional Shareholder Information					
After-Tax Return on Investment	17.2%	21.4%	21.5%	23.5%	21.0%
Return on Average Shareholders' Equity	23.4%	24.9%	24.8%	28.7%	26.8%
Dividends Paid per Share	\$0.665	\$0.575	\$0.410	\$0.320	\$0.268
Shares Outstanding	134.5	140.3	146.0	147.5	150.6
Share Price					
High	\$43.31	\$43.74	\$39.36	\$38.89	\$31.52
Low	\$31.62	\$34.60	\$30.90	\$23.19	\$20.43

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SVP, Industrial Products

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