3M CO
Form 10-K
February 17, 2009
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# UNITED STATES

# SECURITIES AND EXCHANGE COMMISSION

**Washington, D.C. 20549**

# FORM 10-K

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the fiscal year ended December 31, 2008**

**Commission file number 1-3285**

# 3M COMPANY

State of Incorporation: **Delaware** I.R.S. Employer Identification No. **41-0417775**

Principal executive offices: **3M Center, St. Paul, Minnesota 55144**

Telephone number: **(651) 733-1110**

**SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:**

| Title of each class | Name of each exchange on which registered |
|---|---|
| Common Stock, Par Value $.01 Per Share | New York Stock Exchange, Inc. |
| | Chicago Stock Exchange, Inc. |

Note: The common stock of the Registrant is also traded on the SWX Swiss Exchange.

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

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes x No o

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No x

Indicate by 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 o

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. o

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer , accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

| Large accelerated filer x | Accelerated filer o | Non-accelerated filer o<br>(Do not check if a smaller reporting company) | Smaller reporting company o |
|---|---|---|---|

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes o No x

The aggregate market value of voting stock held by nonaffiliates of the Registrant, computed by reference to the closing price and shares outstanding, was approximately $37.3 billion as of January 30, 2009 (approximately $48.6 billion as of June 30, 2008, the last business day of the Registrant s most recently completed second quarter).

Shares of common stock outstanding at January 31, 2009: 693,791,556.

**DOCUMENTS INCORPORATED BY REFERENCE**

Parts of the Company s definitive proxy statement (to be filed pursuant to Regulation 14A within 120 days after Registrant s fiscal year-end of December 31, 2008) for its annual meeting to be held on May 12, 2009, are incorporated by reference in this Form 10-K in response to Part III, Items 10, 11, 12, 13 and 14.

This document (excluding exhibits) contains 104 pages.

The table of contents is set forth on page 2. The exhibit index begins on page 101.

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**3M COMPANY**

**ANNUAL REPORT ON FORM 10-K**

**For the Year Ended December 31, 2008**

# PART I

## Item 1. Business.

3M Company was incorporated in 1929 under the laws of the State of Delaware to continue operations begun in 1902. The Company s ticker symbol is MMM. As used herein, the term 3M or Company includes 3M Company and its subsidiaries unless the context indicates otherwise. In this document, for any references to Note 1 through Note 19, refer to the Notes to Consolidated Financial Statements in Item 8.

### Available Information

The SEC maintains a website that contains reports, proxy and information statements, and other information regarding issuers, including the Company, that file electronically with the SEC. The public can obtain any documents that the Company files with the SEC at http://www.sec.gov. The Company files annual reports, quarterly reports, proxy statements and other documents with the Securities and Exchange Commission (SEC) under the Securities Exchange Act of 1934 (Exchange Act). The public may read and copy any materials that the Company files with the SEC at the SEC s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330.

3M also makes available free of charge through its website (http://investor.3M.com) the Company s Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and, if applicable, amendments to those reports filed or furnished pursuant to the Exchange Act as soon as reasonably practicable after the Company electronically files such material with, or furnishes it to, the SEC.

### General

3M is a diversified technology company with a global presence in the following businesses: Industrial and Transportation; Health Care; Safety, Security and Protection Services; Consumer and Office; Display and Graphics; and Electro and Communications. 3M is among the leading manufacturers of products for many of the markets it serves. Most 3M products involve expertise in product development, manufacturing and marketing, and are subject to competition from products manufactured and sold by other technologically oriented companies.

At December 31, 2008, the Company employed 79,183 people (full-time equivalents), with 33,662 employed in the United States and 45,521 employed internationally.

**Business Segments**

As discussed in Note 17 to the Consolidated Financial Statements, effective in the first quarter of 2008, 3M made certain product moves between its business segments in its continuing effort to drive growth by aligning businesses around markets and customers. Segment information presented herein reflects the impact of these changes for all periods presented.

3M continues to manage its operations in six operating business segments: Industrial and Transportation; Health Care; Safety, Security and Protection Services; Consumer and Office; Display and Graphics; and Electro and Communications. 3M s six business segments bring together common or related 3M technologies, enhancing the development of innovative products and services and providing for efficient sharing of business resources. These segments have worldwide responsibility for virtually all 3M product lines. Certain small businesses and lab-sponsored products, as well as various corporate assets and expenses, are not attributed to the business segments. Financial information and other disclosures relating to 3M s business segments and operations in major geographic areas are provided in the Notes to Consolidated Financial Statements.

*Industrial and Transportation Business:* The Industrial and Transportation segment serves a broad range of markets, such as appliance, paper and packaging, food and beverage, electronics, automotive original equipment manufacturer (OEM) and automotive aftermarket (auto body shops and retail). Industrial and Transportation products include tapes, a wide variety of coated and non-woven abrasives, adhesives, specialty materials, filtration products, closure systems for personal hygiene products, and components and products that are used in the manufacture, repair and maintenance of automotive, marine, aircraft and specialty vehicles. The August 2005 acquisition of CUNO, Incorporated ( CUNO ) added a comprehensive line of filtration products for the separation, clarification and purification of fluids and gases.

Major industrial products include vinyl, polyester, foil and specialty industrial tapes and adhesives; Scotch® Masking Tape, Scotch® Filament Tape and Scotch® Packaging Tape; packaging equipment; 3M VHB Bonding Tapes; conductive, low surface energy, hot melt, spray and structural adhesives; reclosable fasteners; label materials for durable goods; and coated, nonwoven and microstructured surface finishing and grinding abrasives for the industrial market. Other products include a comprehensive line of filtration products for the separation, clarification and purification of

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fluids and gases; fluoroelastomers for seals, tubes and gaskets in engines; engineering fluids; and closures for disposable diapers.

Major transportation products include insulation components, including components for catalytic converters; functional and decorative graphics; abrasion-resistant films; masking tapes; fasteners and tapes for attaching nameplates, trim, moldings, interior panels and carpeting; coated, nonwoven and microstructured finishing and grinding abrasives; structural adhesives; and other specialty materials. In addition, 3M provides paint finishing and detailing products, including a complete system of cleaners, dressings, polishes, waxes and other products.

*Health Care Business:* The Health Care segment serves markets that include medical clinics and hospitals, pharmaceuticals, dental and orthodontic practitioners, and health information systems. Products and services provided to these and other markets include medical and surgical supplies, skin health and infection prevention products, drug delivery systems, dental and orthodontic products, health information systems and anti-microbial solutions. As discussed in Note 2, the global branded pharmaceuticals business was sold in December 2006 and January 2007.

In the medical and surgical areas, 3M is a supplier of medical tapes, dressings, wound closure products, orthopedic casting materials, electrodes and stethoscopes. In infection prevention, 3M markets a variety of surgical drapes, masks and preps, as well as sterilization assurance equipment. Other products include drug delivery systems, such as metered-dose inhalers, transdermal skin patches and related components. Dental and orthodontic products include restoratives, adhesives, finishing and polishing products, crowns, impression materials, preventive sealants, professional tooth whiteners, prophylaxis and orthodontic appliances. In health information systems, 3M develops and markets computer software for hospital coding and data classification, and provides related consulting services. 3M provides microbiology products that make it faster and easier for food processors to test the microbiological quality of food.

*Safety, Security and Protection Services Business:* The Safety, Security and Protection Services segment serves a broad range of markets that increase the safety, security and productivity of workers, facilities and systems. Major product offerings include personal protection products, safety and security products, energy control products, cleaning and protection products for commercial establishment s, track and trace solutions, and roofing granules for asphalt shingles. In August 2006, 3M completed the acquisition of Security Printing and Systems Limited, a producer of finished, personalized passports and secure cards, which expanded the 3M product line related to border and civil security solutions. In April 2008, 3M acquired Aearo Holding Corp., the parent company of Aearo Technologies Inc. (hereafter referred to as Aearo). Aearo manufactures and sells personal protection and energy absorbing products, which expanded 3M s platform by adding hearing protection as well as eyewear and fall protection product lines to 3M s existing line of respiratory products.

This segment s products include certain maintenance-free and reusable respirators, personal protective equipment, electronic surveillance products, films that protect against counterfeiting, and reflective materials that are widely used on apparel, footwear and accessories, enhancing visibility in low-light situations. 3M s Track and Trace Solutions business utilizes radio frequency identification (RFID) technology to provide a growing array of solutions from library patron self-checkout systems to tracking packages. Other products include spill-control sorbents; Thinsulate Insulation and Thinsulate Lite Loft Insulation; 3M Scotchtint Window Film for buildings; 3M Ultra Safety and Security Window Film for property and personal protection during destructive weather conditions; nonwoven abrasive materials for floor maintenance and commercial cleaning; floor matting; and natural and color-coated mineral granules for asphalt shingles. In the second quarter of 2008, 3M completed the sale of its HighJump Software business which provided supply chain execution software solutions.

*Consumer and Office Business:* The Consumer and Office segment serves markets that include consumer retail, office retail, home improvement, building maintenance and other markets. Products in this segment include office supply products, stationery products, construction and home improvement products, home care products, protective material products and consumer health care products.

Major consumer and office products include Scotch® brand products, such as Scotch® Magic   Tape, Scotch® Glue Stick and Scotch® Cushioned Mailer; Post-it® Products, such as Post-it® Flags, Post-it® Note Pads, Post-it® Labeling & Cover-up Tape, and Post-it® Pop-up Notes and Dispensers; construction and home improvement products, including surface-preparation and wood-finishing materials, Command Adhesive Products and Filtrete   Filters for furnaces and air conditioners; home care products, including Scotch-Brite® Scour Pads, Scotch-Brite® Scrub Sponges, Scotch-Brite   Microfiber Cloth products, O-Cel-O   Sponges and Scotchgard   Fabric Protectors; protective material products; certain maintenance-free respirators; and Nexcare   Adhesive Bandages.

*Display and Graphics Business:* The Display and Graphics segment serves markets that include electronic display, traffic safety and commercial graphics. This segment includes optical film solutions for electronic displays; computer screen

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filters; reflective sheeting for transportation safety; commercial graphics systems; and projection systems, including mobile display technology and visual systems products.

The optical film business provides films that serve numerous market segments of the electronic display industry. 3M provides distinct products for five market segments, including products for: 1) LCD computer monitors, 2) LCD televisions, 3) hand-held devices such as cellular phones, 4) notebook PCs and 5) automotive displays. Other optical products include desktop and notebook computer screen filters that address needs for light control, privacy viewing and glare reduction. In traffic safety systems, 3M provides reflective sheetings used on highway signs, vehicle license plates, construction work-zone devices, trucks and other vehicles, and also provides pavement marking systems. Major commercial graphics products include films, inks, digital signage systems and related products used to produce graphics for vehicles and signs. The projection systems business focuses on bringing technology to the projection market, including mobile display technology in addition to its visual communication products that serve the world s office and education markets with overhead projectors and transparency films, as well as equipment and materials for electronic and multimedia presentations.

*Electro and Communications Business:* The Electro and Communications segment serves the electrical, electronics and communications industries, including electrical utilities; electrical construction, maintenance and repair; original equipment manufacturer (OEM) electrical and electronics; computers and peripherals; consumer electronics; telecommunications central office, outside plant and enterprise; as well as aerospace, military, automotive and medical markets; with products that enable the efficient transmission of electrical power and speed the delivery of information and ideas. Products include electronic and interconnect solutions, microinterconnect systems, high-performance fluids, high-temperature and display tapes, telecommunications products, electrical products, and touch screens and touch monitors.

Major electronic and electrical products include packaging and interconnection devices; high-performance fluids used in the manufacture of computer chips, and for cooling electronics and lubricating computer hard disk drives; high- temperature and display tapes; insulating materials, including pressure-sensitive tapes and resins; and related items. 3M Flexible Circuits use electronic packaging and interconnection technology, providing more connections in less space, and are used in ink-jet print cartridges, cell phones and electronic devices. This segment serves the world s telecommunications companies with a wide array of products for fiber-optic and copper-based telecommunications systems for rapid deployment in fixed and wireless networks. The 3M Aluminum Conductor Composite Reinforced (ACCR) electrical power cable, with an aluminum-based metal matrix at its core, increases transmission capacity for existing power lines. The touch systems business includes touch screens and touch monitors.

**Distribution**

3M products are sold through numerous distribution channels, including directly to users and through numerous wholesalers, retailers, jobbers, distributors and dealers in a wide variety of trades in many countries around the world. Management believes the confidence of wholesalers, retailers, jobbers, distributors and dealers in 3M and its products a confidence developed through long association with skilled marketing and sales representatives has contributed significantly to 3M s position in the marketplace and to its growth.

**Research and Patents**

Research and product development constitutes an important part of 3M s activities and has been a major driver of 3M s sales growth. Research, development and related expenses totaled $1.404 billion in 2008, $1.368 billion in 2007 and $1.522 billion in 2006. The global branded pharmaceuticals business, which was divested in December 2006 and January 2007, incurred research, development and related expenses of approximately $120 million in 2006. The 2006 amount also included a $95 million in-process research and development charge (discussed in Note 2) and $75 million in restructuring actions (Note 4). Research and development, covering basic scientific research and the application of scientific advances in the development of new and improved products and their uses, totaled $851 million in 2008, $788 million in 2007 and $943 million in 2006. Related expenses primarily include technical support provided by 3M to customers who are using existing 3M products, and internally developed patent costs, which include costs and fees incurred to prepare, file, secure and maintain patents.

The Company s products are sold around the world under various trademarks that are important to the Company. The Company also owns, or holds licenses to use, numerous U.S. and foreign patents. The Company s research and development activities generate a steady stream of inventions that are covered by new patents. Patents applicable to specific products extend for varying periods according to the date of patent application filing or patent grant and the legal term of patents in the various countries where patent protection is obtained. The actual protection afforded by a patent, which can vary from country to country, depends upon the type of patent, the scope of its coverage and the availability of legal remedies in the country.

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The Company believes that its patents provide an important competitive advantage in many of its businesses. In general, no single patent or group of related patents is in itself essential to the Company as a whole or to any of the Company s business segments.

**Raw Materials**

In 2008, the Company experienced cost increases affecting metals, wood pulp and oil-derived raw materials. To date, the Company is receiving sufficient quantities of all raw materials to meet its reasonably foreseeable production requirements. It is impossible to predict future shortages of raw materials or the impact any such shortages would have. 3M has avoided disruption to its manufacturing operations through careful management of existing raw material inventories and development and qualification of additional supply sources. 3M manages commodity price risks through negotiated supply contracts, price protection agreements and forward physical contracts.

**Environmental Law Compliance**

3M s manufacturing operations are affected by national, state and local environmental laws around the world. 3M has made, and plans to continue making, necessary expenditures for compliance with applicable laws. 3M is also involved in remediation actions relating to environmental matters from past operations at certain sites (refer to Environmental and Other Liabilities and Insurance Receivables in Note 14, Commitments and Contingencies).

Environmental expenditures relating to existing conditions caused by past operations that do not contribute to current or future revenues are expensed. Reserves for liabilities for anticipated remediation costs are recorded on an undiscounted basis when they are probable and reasonably estimable, generally no later than the completion of feasibility studies or the Company s commitment to a plan of action. Environmental expenditures for capital projects that contribute to current or future operations generally are capitalized and depreciated over their estimated useful lives.

In 2008, 3M expended about $26 million for capital projects related to protecting the environment. This amount excludes expenditures for remediation actions relating to existing matters caused by past operations that do not contribute to current or future revenues, which are expensed. Capital expenditures for environmental purposes have included pollution control devices such as wastewater treatment plant improvements, scrubbers, containment structures, solvent recovery units and thermal oxidizers at new and existing facilities constructed or upgraded in the normal course of business. Consistent with the Company s policies stressing environmental responsibility, capital expenditures (other than for remediation projects) for known projects are presently expected to be about $20 million over the next two years for new or expanded programs to build facilities or modify manufacturing processes to minimize waste and reduce emissions.

While the Company cannot predict with certainty the future costs of such cleanup activities, capital expenditures or operating costs for environmental compliance, the Company does not believe they will have a material effect on its capital expenditures, earnings or competitive position.

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**Executive Officers**

Following is a list of the executive officers of 3M, and their age, present position, the year elected to their present position and other positions they have held during the past five years. No family relationships exist among any of the executive officers named, nor is there any undisclosed arrangement or understanding pursuant to which any person was selected as an officer. This information is presented as of the date of the 10-K filing (February 13, 2009).

| Name | Age | Present Position | Year Elected to Present Position | Other Positions Held During 2004-2008 |
|---|---|---|---|---|
| George W. Buckley | 61 | Chairman of the Board, President and Chief Executive Officer | 2005 | Chairman and Chief Executive Officer, Brunswick Corporation, 2000-2005 |
| Patrick D. Campbell | 56 | Senior Vice President and Chief Financial Officer | 2002 | |
| Joe E. Harlan | 49 | Executive Vice President, Electro and Communications Business | 2004 | President and Chairman of the Board, Sumitomo 3M Limited, 2003-2004 |
| Michael A. Kelly | 52 | Executive Vice President, Display and Graphics Business | 2006 | Division Vice President, Occupational Health and Environmental Safety Division, 2003-2006 |
| Angela S. Lalor | 43 | Senior Vice President, Human Resources | 2006 | Staff Vice President, Human Resources Operations, 2005<br>Executive Director, Human Resources Operations, 2004-2005<br>Director, Compensation and Employee Administration, 2002-2004 |
| Jean Lobey | 56 | Executive Vice President, Safety, Security and Protection Services Business | 2005 | Managing Director, 3M Brazil, 2003-2004 |
| Robert D. MacDonald | 58 | Senior Vice President, Marketing and Sales | 2004 | Division Vice President, Automotive Aftermarket Division, 2002-2004 |
| Moe S. Nozari | 66 | Executive Vice President, Consumer and Office Business | 2002 | |
| Frederick J. Palensky | 59 | Executive Vice President, Research and Development and Chief Technology Officer | 2006 | Executive Vice President, Enterprise Services, 2005-2006<br>Executive Vice President, Safety, Security and Protection Services Business, 2002-2005 |
| Brad T. Sauer | 49 | Executive Vice President, Health Care Business | 2004 | Executive Vice President, Electro and Communications Business, 2002-2004 |
| Hak Cheol Shin | 51 | Executive Vice President, Industrial and Transportation Business | 2006 | Executive Vice President, Industrial Business, 2005 |

| | | | | |
|---|---|---|---|---|
| | | | | Division Vice President, Industrial Adhesives and Tapes Division, 2003-2005 |
| Marschall I. Smith | 64 | Senior Vice President, Legal Affairs and General Counsel | 2007 | Vice President and General Counsel Brunswick Corporation, 2001-2007 |
| Inge G. Thulin | 55 | Executive Vice President, International Operations | 2004 | Vice President, Asia Pacific; and Executive Vice President, International Operations, 2003-2004 |
| John K. Woodworth | 57 | Senior Vice President, Corporate Supply Chain Operations | 2006 | Vice President, Asia Pacific, 2004-2006 Division Vice President, Electronic Solutions Division, 2003-2004 |

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**Item 1A. Risk Factors**

Our disclosure and analysis in this Annual Report on Form 10-K contain forward-looking statements that relate to future events and typically address the Company s expected future business and financial performance based on certain assumptions. These assumptions and expectations of future events and trends are subject to risks and uncertainties. Depending on a variety of factors, actual future results and trends may differ materially from historical results or those reflected in any such forward-looking statements. Provided below is a cautionary discussion of what we believe to be the most significant risk factors applicable to the Company. Discussion of these factors is incorporated by reference into and considered an integral part of Part II, Item 7, Management s Discussion and Analysis of Financial Conditions and Results of Operations.

* *Results are impacted by the effects of, and changes in, worldwide economic and capital markets conditions.* The Company operates in more than 60 countries and derives approximately 64 percent of its revenues from outside the United States. The Company s business may be adversely affected by factors in the United States and other countries that are beyond its control, such as disruptions in financial markets or downturns in economic activity in specific countries or regions, or in the various industries in which the Company operates; social, political or labor conditions in specific countries or regions; or adverse changes in the availability and cost of capital, interest rates, tax rates, or regulations in the jurisdictions in which the Company operates.

* *The Company s credit ratings are important to 3M s cost of capital.* The major rating agencies routinely evaluate the Company s credit profile and have assigned debt ratings to 3M that are near the top of the ratings spectrum. This evaluation is based on a number of factors, which include financial strength, business and financial risk, as well as transparency with rating agencies and timeliness of financial reporting. The Company has an AA credit rating, with a stable outlook, from Standard & Poor s and an Aa1 credit rating, with a negative outlook, from Moody s Investors Service. The Company s strong ratings serve to lower 3M s borrowing costs and facilitate access to a variety of lenders. Failure to maintain the current ratings level could adversely affect the Company s cost of funds, liquidity and access to capital markets.

* *The Company s results are affected by competitive conditions and customer preferences.* Demand for the Company s products, which impacts revenue and profit margins, is affected by (i) the development and timing of the introduction of competitive products; (ii) the Company s response to downward pricing to stay competitive; (iii) changes in customer order patterns, such as changes in the levels of inventory maintained by customers and the timing of customer purchases which may be affected by announced price changes, changes in the Company s incentive programs, or the customer s ability to achieve incentive goals; and (iv) changes in customers preferences for our products, including the success of products offered by our competitors, and changes in customer designs for their products that can affect the demand for some of the Company s products.

* *Foreign currency exchange rates and fluctuations in those rates may affect the Company s ability to realize projected growth rates in its sales and earnings.* Because the Company s financial statements are denominated in U.S. dollars and approximately 64 percent of the Company s revenues are derived from outside the United States, the Company s results of operations and its ability to realize projected growth rates in sales and earnings could be adversely affected if the U.S. dollar strengthens significantly against foreign currencies.

* *The Company s growth objectives are largely dependent on the timing and market acceptance of its new product offerings, including its ability to continually renew its pipeline of new products and to bring those products to market.* This ability may be adversely affected by difficulties or delays in product development, such as the inability to identify viable new products, obtain adequate intellectual property protection, or gain market acceptance of new products. There are no guarantees that new products will prove to be commercially successful.

** The Company s future results are subject to fluctuations in the costs and availability of purchased components, compounds, raw materials and energy, including oil and natural gas and their derivatives, due to shortages, increased demand, supply interruptions, currency exchange risks, natural disasters and other factors.* The Company depends on various components, compounds, raw materials, and energy (including oil and natural gas and their derivatives) supplied by others for the manufacturing of its products. It is possible that any of its supplier relationships could be interrupted due to natural and other disasters and other events, or be terminated in the future. Any sustained interruption in the Company s receipt of adequate supplies could have a material adverse effect on the Company. In addition, while the Company has a process to minimize volatility in component and material pricing, no assurance can be given that the Company will be able to successfully manage price fluctuations or that future price fluctuations or shortages will not have a material adverse effect on the Company.

** Acquisitions, strategic alliances, divestitures, and other unusual events resulting from portfolio management actions and other evolving business strategies, and possible organizational restructuring could affect future results.* The Company monitors its business portfolio and organizational structure and has made and may continue to make acquisitions, strategic alliances, divestitures and changes to its organizational structure. With respect to acquisitions, future results will be affected by the Company s ability to integrate acquired businesses quickly and obtain the anticipated synergies.

** The Company s future results may be affected if the Company generates fewer productivity improvements than estimated.* The Company utilizes various tools, such as Lean Six Sigma, to improve operational efficiency and productivity. There can be no assurance that all of the projected productivity improvements will be realized.

** The Company s future results may be affected by various legal and regulatory proceedings, including those involving product liability, antitrust, environmental or other matters.* The outcome of these legal proceedings may differ from the Company s expectations because the outcomes of litigation, including regulatory matters, are often difficult to reliably predict. Various factors or developments can lead the Company to change current estimates of liabilities and related insurance receivables where applicable, or make such estimates for matters previously not susceptible of reasonable

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estimates, such as a significant judicial ruling or judgment, a significant settlement, significant regulatory developments or changes in applicable law. A future adverse ruling, settlement or unfavorable development could result in future charges that could have a material adverse effect on the Company s results of operations or cash flows in any particular period. For a more detailed discussion of the legal proceedings involving the Company and the associated accounting estimates, see the discussion in Note 14.

**Item 1B. Unresolved Staff Comments.**

None.

**Item 2. Properties.**

3M s general offices, corporate research laboratories, and certain division laboratories are located in St. Paul, Minnesota. The Company operates 82 manufacturing facilities in 29 states. The Company operates 102 manufacturing and converting facilities in 35 countries outside the United States.

3M owns substantially all of its physical properties. 3M s physical facilities are highly suitable for the purposes for which they were designed. Because 3M is a global enterprise characterized by substantial intersegment cooperation, properties are often used by multiple business segments.

**Item 3. Legal Proceedings.**

Discussion of legal matters is incorporated by reference from Part II, Item 8, Note 14, Commitments and Contingencies, of this document, and should be considered an integral part of Part I, Item 3, Legal Proceedings.

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

None in the quarter ended December 31, 2008.

**PART II**

**Item 5. Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.**

Equity compensation plans information is incorporated by reference from Part III, Item 12, Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters, of this document, and should be considered an integral part of Item 5. At January 30, 2009, there were 116,366 shareholders of record. 3M s stock is listed on the New York Stock Exchange, Inc. (NYSE), the Chicago Stock Exchange, Inc., and the SWX Swiss Exchange. Cash dividends declared and paid totaled $.50 per share for each quarter of 2008, and $.48 per share for each quarter of 2007. Stock price comparisons follow:

**Stock price comparisons (NYSE composite transactions)**

| (Per share amounts) | First Quarter | Second Quarter | Third Quarter | Fourth Quarter | Year |
|---|---|---|---|---|---|
| **2008 High** | **$ 84.76** | **$ 83.22** | **$ 74.71** | **$ 68.31** | **$ 84.76** |
| **2008 Low** | **72.05** | **68.61** | **65.51** | **50.01** | **50.01** |
| 2007 High | $ 79.88 | $ 89.03 | $ 93.98 | $ 97.00 | $ 97.00 |
| 2007 Low | 72.90 | 75.91 | 83.21 | 78.98 | 72.90 |

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**Issuer Purchases of Equity Securities**

Repurchases of common stock are made to support the Company s stock-based employee compensation plans and for other corporate purposes. In February 2007, 3M s Board of Directors authorized a two-year share repurchase of up to $7.0 billion for the period from February 12, 2007 to February 28, 2009. In February 2009, 3M s Board of Directors extended this share repurchase authorization until the remaining $2.6 billion (as of December 31, 2008) is fully utilized.

**Issuer Purchases of Equity**

**Securities (registered pursuant to**

**Section 12 of the Exchange Act)**

| **Period** | **Total Number of Shares Purchased(1)** | | **Average Price Paid per Share** | **Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs** | | **Maximum Approximate Dollar Value of Shares that May Yet Be Purchased under the Plans or Programs (Millions)** |
|---|---|---|---|---|---|---|
| January 1-31, 2008 | 1,876,312 | $ | 78.23 | 1,871,200 | **$** | **4,002** |
| February 1-29, 2008 | 2,281,560 | $ | 79.37 | 2,201,400 | **$** | **3,828** |
| March 1-31, 2008 | 2,153,150 | $ | 78.28 | 2,126,600 | **$** | **3,662** |
| Total January 1 March 31, 2008 | 6,311,022 | $ | 78.66 | 6,199,200 | **$** | **3,662** |
| April 1-30, 2008 | 2,148,930 | $ | 78.82 | 2,103,100 | **$** | **3,496** |
| May 1-31, 2008 | 2,436,300 | $ | 77.12 | 2,368,400 | **$** | **3,313** |
| June 1-30, 2008 | 3,591,969 | $ | 73.42 | 3,586,500 | **$** | **3,050** |
| Total April 1 June 30, 2008 | 8,177,199 | $ | 75.94 | 8,058,000 | **$** | **3,050** |
| July 1-31, 2008 | 2,507,271 | $ | 69.33 | 2,499,900 | **$** | **2,876** |
| August 1-31, 2008 | 2,036,795 | $ | 71.85 | 2,026,400 | **$** | **2,731** |
| September 1-30, 2008 | 2,183,018 | $ | 69.41 | 2,182,100 | **$** | **2,579** |
| Total July 1 September 30, 2008 | 6,727,084 | $ | 70.12 | 6,708,400 | **$** | **2,579** |
| October 1-31, 2008 | 198,338 | $ | 66.14 | 190,000 | **$** | **2,567** |
| November 1-30, 2008 | 6,196 | $ | 58.83 | | **$** | **2,567** |
| December 1-31, 2008 | 4,163 | $ | 57.13 | | **$** | **2,567** |
| Total October 1 Dec. 31, 2008 | 208,697 | $ | 65.75 | 190,000 | **$** | **2,567** |
| Total January 1 December 31, 2008 | 21,424,002 | $ | 74.81 | 21,155,600 | **$** | **2,567** |

(1) The total number of shares purchased includes: (i) shares purchased under the Board s authorizations described above, and (ii) shares purchased in connection with the exercise of stock options (which totaled 5,112 shares in January 2008, 80,160 shares in February 2008, 26,550 shares in March 2008, 45,830 shares in April 2008, 67,900 shares in May 2008, 5,469 shares in June 2008, 7,371 shares in July 2008, 10,395 shares in August 2008, 918 shares in September 2008, 8,338 shares in October 2008, 6,196 shares in November 2008, and 4,163 shares in December 2008).

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**Item 6. Selected Financial Data.**

| (Dollars in millions, except per share amounts) | 2008 | 2007 | 2006 | 2005 | 2004 |
|---|---|---|---|---|---|
| Years ended December 31: | | | | | |
| Net sales | **$ 25,269** | $ 24,462 | $ 22,923 | $ 21,167 | $ 20,011 |
| Income before cumulative effect of accounting change | **3,460** | 4,096 | 3,851 | 3,146 | 2,841 |
| Per share of common stock: | | | | | |
| Income before cumulative effect of accounting change basic | **4.95** | 5.70 | 5.15 | 4.11 | 3.64 |
| Income before cumulative effect of accounting change diluted | **4.89** | 5.60 | 5.06 | 4.03 | 3.56 |
| Cash dividends declared and paid | **2.00** | 1.92 | 1.84 | 1.68 | 1.44 |
| At December 31: | | | | | |
| Total assets | **$ 25,547** | $ 24,694 | $ 21,294 | $ 20,541 | $ 20,723 |
| Long-term debt (excluding portion due within one year) and long-term capital lease obligations | **5,224** | 4,088 | 1,112 | 1,368 | 798 |

The above income and earnings per share information exclude a cumulative effect of accounting change in 2005 ($35 million, or 5 cents per diluted share). Refer to Note 1 (conditional asset retirement obligations accounting policy) for more detail.

Items included in the preceding table which had a significant impact on results are summarized as follows. 2008 results included net losses that decreased operating income by $269 million and net income by $194 million. 2008 included restructuring actions ($229 million pre-tax, $147 million after-tax and minority interest), exit activities ($58 million pre-tax, $43 million after-tax) and losses related to the sale of businesses ($23 million pre-tax, $32 million after-tax), which were partially offset by a gain on sale of real estate ($41 million pre-tax, $28 million after-tax). 2007 results included net gains that increased operating income by $681 million and net income by $448 million. 2007 included gains related to the sale of businesses ($849 million pre-tax, $550 million after-tax) and a gain on sale of real estate ($52 million pre-tax, $37 million after-tax), which were partially offset by increases in environmental liabilities ($134 million pre-tax, $83 million after-tax), restructuring actions ($41 million pre-tax, $27 million after-tax), and exit activities ($45 million pre-tax, $29 million after-tax). 2006 results included net gains that increased operating income by $523 million and net income by $438 million. 2006 included net benefits from gains related to the sale of certain portions of 3M s branded pharmaceuticals business ($1.074 billion pre-tax, $674 million after-tax) and favorable income tax adjustments ($149 million), which were partially offset by restructuring actions ($403 million pre-tax, $257 million after-tax), acquired in-process research and development expenses ($95 million pre-tax and after-tax), settlement costs of an antitrust class action ($40 million pre-tax, $25 million after-tax), and environmental obligations related to the pharmaceuticals business ($13 million pre-tax, $8 million after-tax). 2005 results included charges that reduced income before cumulative effect of accounting change by $75 million. This related to a tax liability resulting from 3M s reinvestment of approximately $1.7 billion of foreign earnings in the United States pursuant to the repatriation provisions of the American Jobs Creation Act of 2004.

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

Management s Discussion and Analysis of Financial Condition and Results of Operations (MD&A) is designed to provide a reader of 3M s financial statements with a narrative from the perspective of management. 3M s MD&A is presented in nine sections:



**OVERVIEW**

3M is a diversified global manufacturer, technology innovator and marketer of a wide variety of products. As discussed in Note 17 to the Consolidated Financial Statements, effective in the first quarter of 2008, 3M made certain product moves between its business segments. The financial information presented herein reflects the impact of these changes for all periods presented. 3M manages its operations in six operating business segments: Industrial and Transportation; Health Care; Safety, Security and Protection Services; Consumer and Office; Display and Graphics; and Electro and Communications.

3M had record sales in 2008 despite a dramatic fourth-quarter 2008 economic downturn. 3M is responding to this lower demand with aggressive cost and cash management, along with tighter operational discipline. 3M expects to manage through these worldwide market challenges and is positioning itself to benefit when growth returns. 3M streamlined its operations through 2008 and will continue to optimize to protect against the downside throughout 2009. In the fourth quarter of 2008 alone, 3M announced reductions of over 2,400 full-time positions worldwide, which brought total year reductions to approximately 3,500. These job eliminations spanned all sectors and all geographies, but were particularly focused on those developed economies experiencing the most sales pressure. In addition, 3M has furloughed factory workers until production volumes return to more normal levels and contract workers are also being reduced to only those considered essential. These 2008 actions in total are expected to save the Company $250 to $300 million in 2009. 3M also decided to defer merit pay increases in 2009 except in those cases where local laws prohibit it, with estimated cost-avoidance of approximately $100 million in 2009. In addition, 3M has amended its practice on banked vacation effectively phasing it out which will reduce expenses by an estimated $100 million in both 2009 and 2010.

While this market is difficult to predict, in 2009 for planning purposes, 3M is assuming year-on-year declines in organic sales volume, negative foreign currency impacts on sales, operating margin declines, and earnings per share declines. 3M will work to conserve cash by reducing capital expenditures by more than 30 percent in 2009 and by focusing on reducing working capital. 3M has halted stock repurchases until the credit market offers more visibility. The strength of 3M s customer focused diversified business and technology platforms, unparalled geographic reach, and relentless attention to operational excellence, along with 3M s balance sheet strength, provide a strong foundation for stability and consistency in an uncertain global economy.

For the three months ended December 31, 2008, sales decreased 11.2 percent compared to the same period last year, due to an increasingly challenging global economy. Local currency sales (which include volume, selling price and acquisition impacts, but exclude divestiture and translation impacts) increased in Safety, Security and Protection Services and in Health Care. Sales in local currencies for the other four business segments dropped during the fourth quarter. Fourth quarter 2008 net income was $536 million, or $0.77 per diluted share, compared to $851 million, or $1.17 per diluted share in the fourth quarter of 2007. In response to difficult economic conditions, in the fourth-quarter of 2008, 3M took actions which resulted in net pre-tax charges of $219 million for restructuring actions and exit activities, which reduced net income by $140 million, or $0.20 per diluted share, as 3M aggressively balanced its cost structure to a slower growth environment. The fourth quarter of 2007 included net pre-tax charges of $20 million related to restructuring, exit activities and a loss on sale of businesses, which reduced net income by $12 million, or $0.02 per diluted share. Refer to the Special Items summary at the end of this overview section for more detail on these items that impacted results.

For total year 2008, sales increased 3.3 percent to $25.3 billion, with local-currency sales up 1.4 percent. Operating income margins were 20.6 percent, including restructuring and other items that negatively impacted operating income by $269 million, or 1.1 percentage points. In addition to the fourth quarter items noted in the preceding paragraph, refer to the Special Items summary at the end of this overview section for discussion of other items impacting

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results. In 2008, restructuring and other special items negatively impacted net income by $194 million, or $0.28 per diluted share. In 2007, the largest special item was the gain on sale of businesses, primarily the global branded pharmaceuticals business in Europe, which, combined with other items, benefited 2007 net income by $448 million, or $0.62 per diluted share. Including these special items, 3M reported net income of $3.460 billion, or $4.89 per diluted share for 2008, compared to net income of $4.096 billion, or $5.60 per diluted share, for 2007.

In December 2006 and January 2007, 3M completed the sale of its branded pharmaceuticals business, resulting in gains in the fourth quarter of 2006 and first quarter of 2007. In addition, 3M recorded a gain related to the sale of its Opticom Priority Control Systems and Canoga Traffic Detection businesses in the second quarter of 2007. In both 2007 and 2006, these gains on sale of businesses were partially offset by restructuring and the net impact of other special items. Refer to Special Items at the end of this overview section for additional details. Including these special items, in 2007, 3M reported net sales of $24.462 billion and net income of $4.096 billion, or $5.60 per diluted share, compared with net sales of $22.923 billion and net income of $3.851 billion, or $5.06 per diluted share, in 2006. Excluding the special items in both years, the Company still achieved strong underlying operating performance, helped by a 6.7 percent increase in net sales, which included the divestiture impacts discussed above that reduced sales growth by 3.8 percent.

The following table contains sales and operating income results by business segment for the years ended December 31, 2008 and 2007. Refer to the Performance by Business Segment section for discussion of the gain or loss on sale of businesses, restructuring and other items that impacted reported operating income results.

| | 2008 | | | 2007 | | | 2008 vs. 2007 % change | |
|---|---|---|---|---|---|---|---|---|
| **(Dollars in millions)** | **Net Sales** | **% of Total** | **Oper. Income** | **Net Sales** | **% of Total** | **Oper. Income** | **Net Sales** | **Oper. Income** |
| **Business Segments** | | | | | | | | |
| Industrial and Transportation | **$ 7,818** | **30.9%** | **$ 1,477** | $ 7,266 | 29.7% | $ 1,497 | 7.6% | (1.4)% |
| Health Care | **4,293** | **17.0%** | **1,173** | 3,968 | 16.2% | 1,882 | 8.2% | (37.7)% |
| Safety, Security and Protection Services | **3,642** | **14.4%** | **736** | 3,070 | 12.6% | 611 | 18.6% | 20.4% |
| Consumer and Office | **3,448** | **13.6%** | **663** | 3,411 | 13.9% | 692 | 1.1% | (4.1)% |
| Display and Graphics | **3,255** | **12.9%** | **580** | 3,904 | 16.0% | 1,163 | (16.6)% | (50.1)% |
| Electro and Communications | **2,791** | **11.0%** | **531** | 2,763 | 11.3% | 492 | 1.0% | 8.0% |
| Corporate and Unallocated | **22** | **0.2%** | **58** | 80 | 0.3% | (144) | | |
| Total Company | **$ 25,269** | **100%** | **$ 5,218** | $ 24,462 | 100% | $ 6,193 | 3.3% | (15.7)% |

In 2008, worldwide sales growth was broad-based, with five of six segments experiencing sales growth for the year. Safety, Security and Protection Services sales growth was led by acquisitions, primarily Aearo, along with organic growth in personal protection solutions, protective window films and cleaning solutions for commercial buildings, and RFID solutions (Track and Trace). Geographic area sales growth in this business segment was strong in every region, helped by Aearo, with organic sales growth led by Asia Pacific and Latin America. Health Care sales growth was strongest in orthodontics, dental and medical, with positive sales growth in all major geographies, led by Asia Pacific and Latin America. Industrial and Transportation had broad-based sales growth across the portfolio and all major geographies, with strong sales growth in industrial adhesives and tapes, automotive aftermarket, abrasives, and closure systems for personal hygiene products. Sales in Consumer and Office were led by the home care and do-it-yourself markets, with sales growth geographically led by Asia Pacific and Latin America. Consumer and Office experienced weakness in 2008 as slowdowns in the U.S. office markets and residential housing markets persist. Electro and Communications sales growth was led by electrical markets and electronic markets materials, with geographic sales growth strongest in Asia Pacific and Latin America. The electronics solutions and communications markets businesses remain soft. 3M also continued to experience declines in the flexible circuits business, where a number of product solutions are going end-of-life. Within Display and Graphics, positive sales growth in Traffic Safety Systems and Commercial Graphics was more than offset by lower sales in Optical Systems. Optical Systems sales were down 34 percent when compared to 2007, resulting in a sales decline for total Display and Graphics of 16.6 percent. Selling price and attachment rate pressure remain intense in segments of the LCD market as OEMs aggressively pursue cost reductions from their component suppliers, including 3M. In addition, demand dropped significantly in November and December of 2008 as numerous orders were canceled for large-size LCD panels due to weak holiday season sales, reflecting the global downturn in consumer and corporate demand. Refer to the Performance by Business Segment section for a more detailed discussion of the results of the respective segments.

Worldwide total sales growth was 3.3 percent in 2008. Local-currency sales growth was 1.4 percent for 2008, including a 3.3 percentage point benefit from acquisitions. Local-currency sales increased 18.3 percent in Safety, Security and Protection Services (including 14.1 percentage points from acquisitions), 6.8 percent in Health Care (including 1.7 percentage points from acquisitions) and 4.6 percent in Industrial and Transportation (including 3.9 percentage points from acquisitions). Local-currency sales declined 0.3 percent in Consumer and Office, 1.7 percent in Electro and Communications and 17.9 percent in Display and Graphics.

In 2007, worldwide total sales increased 6.7 percent. Local-currency sales growth was 7.3 percent, with organic local-currency growth of 4.9 percent (including 0.7 percentage point benefit from pharmaceuticals supply agreements) and acquisitions adding 2.4 percent. Divestitures, primarily the sale of the global branded pharmaceuticals business (Health Care segment), decreased worldwide sales growth by 3.8 percent. The sale of the pharmaceuticals business was not presented as a discontinued operation due to the extent of the projected continuing cash flows from 3M s contractual supply relationship with the buyers in relation to those of the business that was sold.

Geographically, Latin America and Canada led local-currency sales growth in 2008, with a combined increase of 12.8 percent, followed by Europe, Middle East and Africa (hereafter referred to as Europe) with a 2.8 percent increase and the United States with a 2.7 percent increase. Local-currency sales in Asia Pacific declined 5.9 percent. Asia Pacific was negatively impacted by Optical Systems sales, which were down 34 percent in that region. Excluding Optical Systems, Asia Pacific sales increased nearly 6 percent on a local-currency basis. Of the local-currency sales growth, acquisitions contributed 3.2 percent to the combined Latin America and Canada, 3.2 percent to Europe, 5.3 percent to the United States, and 0.8 percent to Asia Pacific. Foreign currency translation positively impacted international sales by 3.4 percent, as the U.S. dollar weakened in aggregate against many currencies in these geographic areas. Foreign currency translation positively impacted Latin America and Canada by 2.4 percent, Europe by 4.0 percent and Asia Pacific by 3.2 percent. In the fourth quarter of 2008, foreign currency negatively impacted international sales by 7.5 percent. While difficult to predict given the current exchange rate volatility, foreign currency is also expected to have a significant negative impact in 2009.

Worldwide operating income for 2008 decreased 15.7 percent year-on-year, with most of this impact due to the year-on-year change in special items discussed at the end of this overview. In the preceding table, Health Care operating income in 2007 included significant gains related to the sale of portions of its pharmaceuticals business in 2007, negatively impacting the 2008 versus 2007 year-on-year comparisons for this business segment. Worldwide operating income margins were 20.6 percent in 2008, including a 1.1 percent penalty from special items in 2008. Operating income for 2007 increased 8.7 percent year-on-year, including a net 2.2 percentage point benefit from the impact of items discussed in Special Items below. Operating income margins were approximately 25 percent in both 2007 and 2006, with special items positively impacting these margins in both years by approximately 2.5 percentage points.

3M generated $4.533 billion of operating cash flow in 2008, an increase of $258 million compared to 2007, which followed an increase of $436 million when comparing 2007 to 2006. In 2008, 2007 and 2006, the Company utilized approximately $1.4 billion of cash each year to pay dividends. In 2008, repurchases of 3M common stock totaled approximately $1.6 billion, compared to $3.2 billion in 2007 and $2.4 billion in 2006. In February 2007, 3M s Board of Directors authorized a two-year share repurchase of up to $7.0 billion for the period from February 12, 2007 to February 28, 2009. As of December 31, 2008, approximately $2.6 billion remained available for repurchase. In February 2009, 3M s Board of Directors extended this share repurchase authorization until the remaining $2.6 billion is fully utilized. With the Company s current emphasis on maintaining ample liquidity and enhancing balance sheet strength, share repurchase activity has been suspended. However, extension of this program will provide flexibility to resume repurchase activity when business conditions permit. In February 2009, 3M s Board of Directors authorized a dividend increase of 2 percent for 2009, marking the 51st consecutive year of dividend increases for 3M. 3M s debt to total capital ratio (total capital defined as debt plus equity) at December 31, 2008 was 40 percent, compared to 30 percent at December 31, 2007. A portion of the increase in debt was the result of a strategy to build and maintain a cash buffer in the U.S. in the current market environment. 3M has an AA credit rating from Standard & Poor s, with a stable outlook, and an Aa1 credit rating from Moody s Investors Service, with a negative outlook. The Company has sufficient access to capital markets to meet currently anticipated growth and acquisition investment funding needs.

In 2008, the Company experienced cost increases affecting metals, wood pulp and oil-derived raw materials. To date the Company is receiving sufficient quantities of all raw materials to meet its reasonably foreseeable production requirements. It is impossible to predict future shortages of raw materials or the impact any such shortages would have. 3M has avoided disruption to its manufacturing operations through careful management of existing raw material inventories and development and qualification of additional supply sources. 3M manages commodity price risks through negotiated supply contracts, price protection agreements and forward physical contracts.

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In 2009, 3M is changing its annual stock option and restricted stock unit grant date to more closely align the award with the timing of the Company s performance review process. In 2009 and forward, under the annual grant, 3M will grant shares in February instead of May as in previous years. Accounting rules requires recognition of expense under a non-substantive vesting period approach, requiring compensation expense recognition when an employee is eligible to retire. 3M employees in the United States are eligible to retire at age 55 and after having completed five years of service. Approximately 25 percent of the stock-based compensation award expense dollars are for this retiree-eligible population. Therefore, in 2006, 2007 and 2008 the second quarter of each year (because of the May grant date) reflected higher stock-based compensation expense than the other quarters. In 2009, the retiree-eligible impact will shift to the first quarter of 2009. In addition, both the first and second quarter of 2009 will reflect accelerated stock-based compensation expense related to the earlier February grant date. These and other factors result in a first quarter 2009 estimate of $0.08 per diluted share for stock-based compensation expense compared to $0.04 in the first quarter of 2008. In the second quarter of 2009 estimated stock-based compensation is estimated at $0.04 per diluted share compared to $0.06 in the second quarter of 2008. Refer to Note 16 for additional discussion of the Company s stock-based compensation programs.

During 2008 the funded status of the Company s global pension plans declined from 100 percent to 85 percent. As of December 31, 2008, the U.S. pension plans funded status was 89 percent with the qualified plan at 92 percent, and the international plans at 75 percent. By utilizing an effective hedging strategy for both fixed income and equity investments, the Company was able to limit the decline in U.S. pension plan s assets to a negative 13.6% return in 2008, much better than the overall market. In 2009, the Company expects to contribute an amount in the range of $600 million to $850 million to its U.S. and international pension plans. The Company does not have a required minimum pension contribution obligation for its U.S. plans in 2009. The changes in 3M s defined benefit pension and postretirement plans funded status, which are required to be measured as of each year-end, significantly impacted several balance sheet line amounts at December 31, 2008. In the fourth quarter of 2008, these required annual measurements decreased prepaid pension benefits assets by $1.7 billion, increased deferred taxes within other assets by $1.1 billion, increased pension and postretirement benefits long-term liabilities by $1.7 billion and decreased stockholders equity (reflected after taxes) by $2.3 billion. Other pension and postretirement changes during the year, such as contributions and amortization, also impacted these balance sheet captions. Refer to critical accounting estimates within MD&A and Note 11 (Pension and Postretirement Benefit Plans) for additional information concerning 3M s pension and post-retirement plans.

The preceding forward-looking statements involve risks and uncertainties that could cause results to differ materially from those projected (refer to the forward-looking statements section in Item 7 and the risk factors provided in Item 1A for discussion of these risks and uncertainties).

Special Items:

Special items represent significant charges or credits that are important to understanding changes in the Company s underlying operations.

In 2008, net losses for restructuring and other actions decreased operating income by $269 million and net income by $194 million, or $0.28 per diluted share. 2008 included restructuring actions ($229 million pre-tax, $147 million after-tax and minority interest), exit activities ($58 million pre-tax, $43 million after-tax) and losses related to the sale of businesses ($23 million pre-tax, $32 million after-tax), which were partially offset by a gain on sale of real estate ($41 million pre-tax, $28 million after-tax). Divestiture impacts, restructuring actions and exit activities are discussed in more detail in Note 2 (Acquisitions and Divestitures) and Note 4 (Restructuring Actions and Exit Activities). Concerning the real estate gain, 3M received proceeds and recorded a gain in 2008 for a sale-leaseback transaction relative to an administrative location in Italy. 3M anticipates leasing back the facility through late 2009 at which time a new location will be utilized.

In 2007, gains on sale of businesses and real estate, net of restructuring and other items, increased operating income by $681 million and net income by $448 million, or $0.62 per diluted share. 2007 included net benefits from gains related to the sale of businesses ($849 million pre-tax,

$550 million after-tax) and a gain on sale of real estate ($52 million pre-tax, $37 million after-tax), which were partially offset by increases in environmental liabilities ($134 million pre-tax, $83 million after-tax), restructuring actions ($41 million pre-tax, $27 million after-tax), and other exit activities ($45 million pre-tax, $29 million after-tax). These items, except the gain on sale of real estate, are discussed in more detail in Note 2 (Acquisitions and Divestitures), Note 4 (Restructuring Actions and Exit Activities) and Note 14 (Commitments and Contingencies). Gains on sale of businesses include the second-quarter 2007 sale of 3M s Opticom Priority Control Systems and Canoga Traffic Detection businesses, and the first-quarter 2007 sale of the global branded pharmaceuticals business in Europe. Concerning the real estate sale, 3M sold a laboratory facility located in Suwon, Korea.

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In 2006, gains on sale of businesses, net of restructuring and other items, increased operating income by $523 million and net income by $438 million, or $0.57 per diluted share. 2006 included net benefits from gains related to the sale of certain portions of 3M s branded pharmaceuticals business ($1.074 billion pre-tax, $674 million after-tax) and favorable income tax adjustments ($149 million), which were partially offset by restructuring actions ($403 million pre-tax, $257 million after-tax), acquired in-process research and development expenses ($95 million pre-tax and after-tax), settlement costs of an antitrust class action ($40 million pre-tax, $25 million after-tax), and environmental obligations related to the pharmaceuticals business ($13 million pre-tax, $8 million after-tax). These items, except the settlement costs and environmental obligations, are discussed in more detail in Note 2 (Acquisitions and Divestitures), Note 4 (Restructuring Actions and Exit Activities) and Note 8 (Income Taxes). Concerning settlement costs, the Company recorded $40 million in 2006 with respect to a settlement in principle related to the antitrust class action brought on behalf of direct purchasers who did not purchase private label tape. Concerning environmental obligations, the Company increased its reserves by $13 million during 2006 for estimated environmental remediation costs at a European pharmaceutical plant.

**RESULTS OF OPERATIONS**

***Net Sales:***

| | 2008 U.S. | 2008 Intl. | 2008 Worldwide | 2007 U.S. | 2007 Intl. | 2007 Worldwide |
|---|---|---|---|---|---|---|
| Net sales (millions) | $ 9,179 | $ 16,090 | $ 25,269 | $ 8,987 | $ 15,475 | $ 24,462 |
| % of worldwide sales | 36.3% | 63.7% | | 36.7% | 63.3% | |
| Components of net sales change: | | | | | | |
| Volume organic | (5.0)% | (1.0)% | (2.4)% | 1.6% | 7.4% | 5.1% |
| Volume acquisitions | 5.3 | 2.2 | 3.3 | 3.1 | 2.1 | 2.4 |
| Price | 2.4 | (0.5) | 0.5 | 1.0 | (1.1) | (0.2) |
| Local-currency sales (including acquisitions) | 2.7 | 0.7 | 1.4 | 5.7 | 8.4 | 7.3 |
| Divestitures | (0.6) | (0.1) | (0.3) | (4.2) | (3.6) | (3.8) |
| Translation | | 3.4 | 2.2 | | 5.2 | 3.2 |
| Total sales change | 2.1% | 4.0% | 3.3% | 1.5% | 10.0% | 6.7% |

In 2008, local-currency sales growth of 1.4 percent was led by the Safety, Security and Protection Services; Health Care; and Industrial and Transportation segments. Acquisitions increased 2008 sales by 3.3 percent, led by the April 2008 acquisition of Aearo. In 2007, local-currency sales growth of 7.3 percent was led by the Health Care; Safety, Security and Protection Services; Industrial and Transportation and Consumer and Office segments. Acquisitions increased 2007 sales by 2.4 percent, led by the August 2006 acquisition of Security Printing and Systems Limited and the late 2006 acquisitions of Softmed Systems Inc. and Biotrace International PLC. Refer to both the Performance by Business Segment and Performance by Geographic Area sections for additional discussion of sales change.

***Operating Expenses:***

| (Percent of net sales) | 2008 | 2007 | 2006 | 2008 Versus 2007 | 2007 Versus 2006 |
|---|---|---|---|---|---|
| Cost of sales | **52.9%** | 52.1% | 51.1% | 0.8% | 1.0% |
| Selling, general and administrative expenses | **20.8** | 20.5 | 22.1 | 0.3 | (1.6) |

| | | | | | |
|---|---|---|---|---|---|
| Research, development and related expenses | **5.6** | 5.6 | 6.6 | | (1.0) |
| (Gain)/loss on sale of businesses | **0.1** | (3.5) | (4.6) | 3.6 | 1.1 |
| Operating income | **20.6%** | 25.3% | 24.8% | (4.7)% | 0.5% |

As discussed in the preceding overview section, in 2008 the combination of restructuring actions, exit activities and a loss on sale of businesses, partially offset by a gain on sale of real estate, decreased operating income by $269 million, or 1.1 percent of net sales. In 2007, the gain on sale of businesses and real estate, net of environmental liability charges, restructuring and exit activities, benefited 2007 operating income by $681 million, or 2.8 percent of net sales. In 2006, the gain on sale of businesses, net of restructuring and other items, benefited 2006 operating income by $523 million, or 2.2 percent of net sales. The following tables summarize these items by operating expense category. Items included in the Other category of the table for 2006 are acquired in-process research and development expenses ($95 million), settlement costs of a antitrust class action ($40 million), and environmental obligations related to the pharmaceuticals business ($13 million).

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2008 Restructuring and Other Summary

| (Millions) | Restructuring actions | Exit activities | Loss on sale of businesses | Gain on sale of real estate | Total |
|---|---|---|---|---|---|
| Cost of sales | $ 84 | $ 38 | $ | $ | $ 122 |
| Selling, general and administrative expenses | 135 | 17 | | (41) | 111 |
| Research, development and related expenses | 10 | 3 | | | 13 |
| Loss on sale of businesses | | | 23 | | 23 |
| Total operating income penalty (benefit) | $ 229 | $ 58 | $ 23 | $ (41) | $ 269 |

2007 Gain on Sale, Restructuring and Other Summary

| (Millions) | Gain on Sale of businesses | Environ-mental liabilities | Restructuring and exit activities | Gain on sale of real estate | Total |
|---|---|---|---|---|---|
| Cost of sales | $ | $ | $ 64 | $ | $ 64 |
| Selling, general and administrative expenses | | 134 | 26 | (52) | 108 |
| Research, development and related expenses | | | (4) | | (4) |
| Gain on sale of businesses | (849) | | | | (849) |
| Total operating income penalty (benefit) | $ (849) | $ 134 | $ 86 | $ (52) | $ (681) |

2006 Gain on Sale, Restructuring and Other Summary

| (Millions) | Gain on sale of pharmaceuticals business | Pharmaceuticals restructuring actions | Overhead reduction actions | Business specific actions | Total restructuring actions | Other | Total |
|---|---|---|---|---|---|---|---|
| Cost of sales | $ | $ 32 | $ 24 | $ 74 | $ 130 | $ 13 | $ 143 |
| Selling, general and administrative expenses | | 66 | 81 | 51 | 198 | 40 | 238 |
| Research, development and related expenses | | 68 | 7 | | 75 | 95 | 170 |
| Gain on sale of businesses | (1,074) | | | | | | (1,074) |
| Total operating income penalty (benefit) | $ (1,074) | $ 166 | $ 112 | $ 125 | $ 403 | $ 148 | $ (523) |

***Cost of Sales:***

Cost of sales includes manufacturing, engineering and freight costs. Cost of sales as a percent of net sales increased 0.8 percentage points in 2008 compared to 2007, with this increase primarily due to the decline in Optical Systems sales and the rapid volume declines of certain other businesses in the fourth quarter. For the majority of the year 3M s broad-based portfolio performed as expected, with benefits from selling price increases, foreign currency translation, and a continuous focus on driving operational excellence, helping to offset raw material inflation of approximately 4 percent for 2008, compared with 2007. In 2008, restructuring and exit costs increased cost of sales by $122 million, or 0.4 percentage points as a percent of net sales, similar to the 0.3 percentage point impact in 2007, as discussed below.

Cost of sales as a percent of net sales increased 1.0 percentage point in 2007 compared to 2006, with this increase primarily due to the sale of the branded pharmaceuticals business, which had lower than average cost of sales. Raw material costs increased approximately 1 percent in 2007, compared with 2006. In 2007, restructuring and exit costs increased cost of sales by $64 million, or 0.3 percentage points. These charges primarily related to the consolidation of certain flexible circuit manufacturing operations, the phaseout of operations at the Company s New Jersey roofing granule facility and charges related to the Company s decision to close an Electro and Communications facility in Wisconsin. In 2006, restructuring and other items increased cost of sales by $143 million, or 0.7 percentage points.

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***Selling, General and Administrative Expenses:***

Selling, general and administrative (SG&A) expenses as a percent of net sales increased 0.3 percentage points in 2008 when compared to 2007, or 4.6 percent in dollars. In 2008, SG&A expenses related to restructuring actions and exit activities were partially offset by a gain on sale of real estate, which combined increased SG&A by $111 million, or 0.5 percentage points, similar to the 0.4 percentage point impact in 2007, as discussed below. In the fourth quarter of 2008, as part of its restructuring program, 3M took aggressive actions to reduce general and administrative expenses and also pared back selling and marketing costs in certain businesses.

SG&A expenses as a percent of net sales decreased 1.6 percentage points in 2007 when compared to 2006, as expenses incurred in 2006 in the Company s now-divested global branded pharmaceuticals business did not repeat in 2007. Non-pharmaceutical ongoing SG&A expenses, after adjusting for the following items, were up approximately 7 percent in dollars, as the Company invested in sales and marketing to support growth markets. In 2007, SG&A includes increases in environmental liabilities, restructuring charges and exit activities, net of the gain on sale of real estate ($108 million combined net expense), which increased SG&A as a percent of sales by 0.4 percentage points. 2006 included restructuring actions and settlement costs of a previously disclosed antitrust class action ($238 million combined expense), which increased 2006 SG&A as a percent of sales by 1.0 percentage points. In dollars, SG&A decreased $51 million when comparing 2007 to 2006, with the change in restructuring and other items year-on-year decreasing SG&A by $130 million, pharmaceutical SG&A spending decreasing $241 million and other SG&A spending increasing $320 million, or approximately 7 percent in dollars.

***Research, Development and Related Expenses:***

Research, development and related expenses (R&D) in 2008 as a percent of net sales was 5.6 percent, the same as in 2007, while spending in dollars increased. 3M s long-term commitment to R&D is unchanged, but in the current economic environment 3M is closely scrutinizing all discretionary investments.

R&D as a percent of net sales decreased 1.0 percentage point in 2007 when compared to 2006, as expenses incurred in 2006 in the Company s now-divested R&D-intensive pharmaceuticals business did not repeat in 2007. Non-pharmaceutical ongoing R&D expenses, after adjusting for the following items, were up approximately 11 percent in dollars, as the Company invested in future technologies and growth opportunities. 2006 spending included a $95 million in-process research and development charge (discussed in Note 2) and $75 million in restructuring actions (Note 4), which increased 2006 R&D as a percent of sales by 0.7 percentage points. In dollars, R&D spending decreased $154 million when comparing 2007 to 2006, with the change in restructuring and other items year-on-year decreasing R&D by $174 million, 2006 pharmaceutical SG&A spending decreasing $120 million and other R&D spending increasing $140 million, or approximately 11 percent in dollars.

***(Gain)/Loss on Sale of Businesses:***

In June 2008, 3M completed the sale of HighJump Software, a 3M Company, to Battery Ventures, a technology venture capital and private equity firm. 3M received proceeds of $85 million for this transaction and recognized, net of assets sold, transaction and other costs, a pre-tax loss of $23 million (recorded in the Safety, Security and Protection Services segment) in the second quarter of 2008.

In January 2007, 3M completed the sale of its global branded pharmaceuticals business in Europe to Meda AB. 3M received proceeds of $817 million for this transaction and recognized, net of assets sold, a pre-tax gain of $781 million in 2007 (recorded in the Health Care segment). In June 2007, 3M completed the sale of its Opticom Priority Control Systems and Canoga Traffic Detection businesses to TorQuest Partners Inc., a Toronto-based investment firm. 3M received proceeds of $80 million for this transaction and recognized, net of assets sold, transaction and other costs, a pre-tax gain of $68 million (recorded in the Display and Graphics segment) in 2007.

In December 2006, 3M completed the sale of its global branded pharmaceuticals businesses in the United States, Canada, and Latin America region and the Asia Pacific region, including Australia and South Africa. 3M received proceeds of $1.209 billion for these transactions and recognized a pre-tax gain on sale of $1.074 billion in 2006 (recorded in the Health Care segment). For more detail, refer to Note 2.

***Operating Income:***

3M uses operating income as one of its primary business segment performance measurement tools. Operating income decreased in 2008 to 20.6 percent of sales, negatively impacted by restructuring actions, exit activities and a loss on sale of businesses that were partially offset by a gain on sale of real estate, which combined decreased operating income by 1.1 percentage points ($269 million). Operating income margins of 25.3 percent in 2007 were positively impacted by 2.8 percentage points ($681 million) from the gain on sale of businesses and real estate, net of environmental liabilities, restructuring and other exit activities. Operating income margins of 24.8 percent for 2006 were positively impacted by 2.2 percentage points ($523 million) from the gain on sale of portions of the pharmaceuticals business, net of restructuring and other actions. Adjusting for the preceding items, operating income margins in 2007 were similar to 2006.

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***Interest Expense and Income:***

| (Millions) | 2008 | 2007 | 2006 |
|---|---|---|---|
| Interest expense | **$ 215** | $ 210 | $ 122 |
| Interest income | **(105)** | (132) | (51) |
| Total | **$ 110** | $ 78 | $ 71 |

*Interest Expense*: Interest expense increased slightly in 2008 compared to 2007, primarily related to higher average U.S. and international long-term debt balances, which were partially offset by lower short-term debt balances and interest rates. Interest expense increased in 2007 compared to 2006, primarily due to higher average debt balances and higher interest rates.

*Interest Income:* Interest income was lower in 2008 compared to 2007, primarily due to lower interest rates, which were partially offset by higher average cash and cash equivalent balances. Interest income increased in 2007 compared to 2006, primarily due to higher average cash, cash equivalent and marketable securities balances and higher interest rates.

***Provision for Income Taxes:***

| (Percent of pre-tax income) | 2008 | 2007 | 2006 |
|---|---|---|---|
| Effective tax rate | **31.1%** | 32.1% | 30.6% |

The effective tax rate for 2008 was 31.1 percent compared with 32.1 percent in 2007. The Company s 2008 tax rate benefited from reduced international tax rates. The tax rate for 2007 was 32.1 percent compared with 30.6 percent in 2006. The Company s 2006 tax rate included benefits from adjustments to its reserves for tax contingencies following the settlement of income tax audits. Refer to Note 8 for additional information.

***Minority Interest:***

| (Millions) | 2008 | 2007 | 2006 |
|---|---|---|---|
| Minority interest | **$ 60** | $ 55 | $ 51 |

Minority interest expense eliminates the income or loss attributable to non-3M ownership interests in 3M consolidated entities. 3M s most significant consolidated entity with non-3M ownership interests is Sumitomo 3M Limited in Japan (3M owns 75 percent of Sumitomo 3M Limited).

***Currency Effects:***

3M estimates that year-on-year currency effects, including hedging impacts, increased net income by approximately $160 million in 2008, $150 million in 2007 and $20 million in 2006. This estimate includes the effect of translating profits from local currencies into U.S. dollars; the impact of currency fluctuations on the transfer of goods between 3M operations in the United States and abroad; and transaction gains and losses, including derivative instruments designed to reduce foreign currency exchange rate risks other than instruments hedging foreign currency risks on tax obligations. 3M estimates that year-on-year derivative and other transaction gains and losses increased net income by approximately $40 million in 2008, increased net income by approximately $10 million in 2007 and had an immaterial impact on net income in 2006.

**PERFORMANCE BY BUSINESS SEGMENT**

Disclosures relating to 3M s business segments are provided in Item 1, Business Segments. Financial information and other disclosures are provided in the Notes to the Consolidated Financial Statements. As discussed in Note 16 to the Consolidated Financial Statements, effective in the first quarter of 2008, 3M made certain product moves between its business segments in its continuing effort to drive growth by aligning businesses around markets and customers. Segment information presented herein reflects the impact of these changes for all periods presented. The reportable segments are the Industrial and Transportation segment; the Health Care segment; Safety, Security and Protection Services segment; Consumer and Office segment; Display and Graphics segment; and Electro and Communications segment. Information related to 3M s business segments is presented in the tables that follow. Local-currency sales (which include both core and acquisition volume impacts, plus price impacts) are provided for each segment. The divestiture impact, translation impact and total sales change are also provided for each segment.

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As discussed in the preceding overview and results of operations section, the combination of restructuring actions, gains and losses on the sale of businesses, and other special items significantly impacted 2008, 2007 and 2006 results. The following tables summarize these special items by business segment.

**2008 Restructuring and Other Summary**

| (Millions) | Restructuring actions | Exit activities | Loss on sale of businesses | Gain on sale of real estate | Total |
|---|---|---|---|---|---|
| Industrial and Transportation | $ 40 | $ 26 | $ | $ | $ 66 |
| Health Care | 51 | 9 | | | 60 |
| Safety, Security and Protection Services | 12 | 3 | 23 | | 38 |
| Consumer and Office | 18 | | | | 18 |
| Display and Graphics | 24 | 18 | | | 42 |
| Electro and Communications | 7 | | | | 7 |
| Corporate and Unallocated | 77 | 2 | | (41) | 38 |
| Total operating income penalty (benefit) | $ 229 | $ 58 | $ 23 | $ (41) | $ 269 |

**2007 Gain on Sale, Restructuring and Other Summary**

| (Millions) | Gain on sale of businesses | Environmental liabilities | Restructuring and exit activities | Gain on sale of real estate | Total |
|---|---|---|---|---|---|
| Industrial and Transportation | $ | $ | $ 9 | $ | $ 9 |
| Health Care: | | | | | |
| Gain on sale of pharmaceuticals business | (781) | | | | (781) |
| Restructuring actions and other | | | (10) | | (10) |
| Safety, Security and Protection Services | | | 29 | | 29 |
| Consumer and Office | | | | | |
| Display and Graphics | (68) | | 17 | | (51) |
| Electro and Communications | | | 41 | | 41 |
| Corporate and Unallocated | | 134 | | (52) | 82 |
| Total operating income penalty (benefit) | $ (849) | $ 134 | $ 86 | $ (52) | $ (681) |

**2006 Gain on Sale, Restructuring and Other Summary**

| (Millions) | Gain on sale of pharmaceuticals business | Pharmaceuticals restructuring actions | Overhead reduction actions | Business specific actions | Total restructuring actions | Other | Total |
|---|---|---|---|---|---|---|---|
| Industrial and Transportation | $ | $ | $ | $ 15 | $ 15 | $ | $ 15 |
| Health Care: | | | | | | | |
| Gain on sale of pharmaceuticals business | (1,074) | | | | | | (1,074) |
| Restructuring actions and other | | 166 | 112 | 15 | 293 | 108 | 401 |
| Safety, Security and Protection Services | | | | 10 | 10 | | 10 |
| Consumer and Office | | | | | | | |
| Display and Graphics | | | | 31 | 31 | | 31 |
| Electro and Communications | | | | 54 | 54 | | 54 |
| Corporate and Unallocated | | | | | | 40 | 40 |
| Total operating income penalty (benefit) | $ (1,074) | $ 166 | $ 112 | $ 125 | $ 403 | $ 148 | $ (523) |

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Due to the significant impact of the economic downturn in the fourth-quarter of 2008 on sales and operating income results, the following discusses both fourth-quarter 2008 and total year 2008 results for each business segment.

***Industrial and Transportation Business (30.9% of consolidated sales):***

| | 2008 | 2007 | 2006 |
|---|---|---|---|
| Sales (millions) | **$ 7,818** | $ 7,266 | $ 6,632 |
| Sales change analysis: | | | |
| Local currency (volume and price) | **4.6%** | 5.8% | 9.0% |
| Translation | **3.0** | 3.8 | 0.8 |
| Total sales change | **7.6%** | 9.6% | 9.8% |
| | | | |
| Operating income (millions) | **$ 1,477** | $ 1,497 | $ 1,338 |
| Percent change | **(1.4)%** | 11.9% | 11.0% |
| Percent of sales | **18.9%** | 20.6% | 20.2% |

The Industrial and Transportation segment serves a broad range of markets, such as appliance, paper and packaging, food and beverage, electronics, automotive original equipment manufacturer (OEM) and automotive aftermarket (auto body shops and retail). Industrial and Transportation products include tapes, a wide variety of coated and non-woven abrasives, adhesives, specialty materials, filtration products, closure systems for personal hygiene products, and components and products that are used in the manufacture, repair and maintenance of automotive, marine, aircraft and specialty vehicles.

2008 can be characterized as a tale of two distinct chapters for Industrial and Transportation. The first was January through October, characterized by outstanding top-and bottom-line growth across most of the portfolio; the second chapter was the combined months of November and December, when many large customers slowed their operations. 3M expects that the strength of its new products, supply chain improvements and expansion into areas like energy, aerospace, filtration and now renewable energy, will help carry it through some very challenging times.

Among 3M s business segments, Industrial and Transportation has been among those most affected by recent economic contractions, particularly in big industries such as automotive and electronics. With worldwide industrial production in decline, 3M s Industrial and Transportation business had fourth quarter 2008 sales of $1.7 billion, an 11.3 percent decline compared to 2007. Local-currency sales were down 6.3 percent, including a positive 3.2 percent impact from acquisitions. Not all divisions within Industrial were impacted equally in the fourth quarter. Those that are heavily linked to automotive manufacturing, namely automotive OEM and 3M Dyneon, saw declines of more than 20 percent, as did businesses selling to the electronics industry, such as high-tech tapes and adhesives. Most other divisions experienced local-currency sales contractions of less than 10 percent in the fourth quarter. The most significant bright spot in the quarter was the automotive aftermarket business, which contributed solid local-currency growth. Geographically, fourth quarter 2008 local-currency sales were down in all regions, with the largest declines in the U.S. and Asia Pacific, followed by Europe. Local-currency sales were flat in Latin America. Operating income in the fourth quarter declined 42 percent to $203 million, which included net charges of $36 million for restructuring actions and exit activities.

Full-year 2008 sales looked far more positive, with sales up 7.6 percent to $7.8 billion. Local-currency growth rates were strongest in the automotive aftermarket business. 3M also drove strong sales growth in two of its largest divisions, namely abrasives and industrial tapes and adhesives. Closure systems for personal hygiene products also showed good growth. Geographically, all major regions drove positive local-currency sales growth. Strong market penetration continued in emerging economies, especially the high growth BRICP countries (Brazil, Russia, India, China and Poland), where the business drove strong organic local-currency growth. Operating income declined, but increased after adjusting for $66 million in restructuring actions and exit activities (discussed further below). Strong operational discipline was the key to protecting the bottom line as full-year operating margins totaled 18.9 percent, with operating income margins at 19.7 percent after adjusting for restructuring and exit activities.

Industrial and Transportation restructuring and exit activities totaled $66 million for total year 2008. During the fourth quarter of 2008, restructuring actions totaling $40 million (partially offset by a $4 million reduction in previously accrued exit activity charges) were comprised of severance and related benefits totaling $33 million and asset impairments of $7 million. Net exit activity charges of $26 million in 2008 largely related to employee reductions at an Industrial and Transportation manufacturing facility located in the United Kingdom, which totaled $19 million. This compared to restructuring actions and exit activities of $9 million in 2007.

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Industrial and Transportation continues to invest in innovative new products along with complementary gap-fill acquisitions, evidenced by the closing of eight acquisitions in 2008, with some of the larger acquisitions summarized as follows. In July 2008, 3M acquired K&H Surface Technologies Pty. Ltd., an Australian-based manufacturing company specializing in a range of repair products for the professional do-it-yourself automotive refinish markets. In August 2008, 3M acquired Polyfoam Products Inc., a structural adhesives company specializing in foam adhesives for tile roofing and other adhesive products for the building industry. In October 2008, 3M completed its acquisition of EMFI S.A. and SAPO S.A.S., manufacturers of polyurethane-based structural adhesives and sealants headquartered in Haguenau, France. In October 2008, 3M also completed its acquisition of Meguiar s Inc., a 100-year-old business that manufactures the leading Meguiar s brand of car care products for cleaning and protecting automotive surfaces, which is headquartered in Irvine, California.

In 2007, local-currency sales increased 5.8 percent, including 1.8 percent growth from acquisitions. Sales growth was broad-based, led by industrial adhesives and tapes, automotive aftermarket, abrasives and automotive OEM businesses. All geographic areas contributed positively to growth. Significant manufacturing investments were made in emerging economies such as India, China and Poland to simplify the supply chain and get closer to local customers. Good operational discipline helped deliver operating income growth of 11.9 percent, with operating income margins of 20.6 percent. Operating income in 2007 included $9 million in restructuring and other exit activity expenses, primarily comprised of severance and related benefits. Operating income in 2006 included $15 million in restructuring expenses, primarily comprised of asset impairments and severance and related benefits.

In March 2005, 3M s automotive business completed the purchase of 19 percent of TI&M Beteiligungsgesellschaft mbH (TI&M) for approximately $55 million. TI&M is the parent company of I&T Innovation Technology Entwicklungsund Holding Aktiengesellschaft (I&T), an Austrian maker of flat flexible cable and circuitry. Pursuant to a Shareholders Agreement, 3M marketed the firm s flat flexible wiring systems for automotive interior applications to the global automotive market. I&T filed a petition for bankruptcy protection in August 2006. As part of its agreement to purchase the shares of TI&M, the Company was granted a put option, which gave the Company the right to sell back its entire ownership interest in TI&M to the other investors from whom 3M acquired its 19 percent interest. The put option became exercisable January 1, 2007. The Company exercised the put option and recovered approximately $25 million of its investment from one of the investors based in Belgium in February 2007. The other two TI&M investors have filed a bankruptcy petition in Austria. The Company is pursuing recovery of the balance of its investment both through the Austrian bankruptcy proceedings and pursuant to the terms of the Share Purchase Agreement. The Company received approximately $6 million of its investment back in the fourth quarter of 2008. The Company believes collection of its remaining investment is probable and, as a result, no impairment reserve has been recorded.

***Health Care Business (17.0% of consolidated sales):***

| | **2008** | **2007** | **2006** |
|---|---|---|---|
| Sales (millions) | **$ 4,293** | $ 3,968 | $ 4,011 |
| Sales change analysis: | | | |
| Local currency (volume and price) | **6.8%** | 18.3% | 6.0% |
| Divestitures | **(0.1)** | (23.7) | |
| Translation | **1.5** | 4.3 | 0.7 |
| Total sales change | **8.2%** | (1.1)% | 6.7% |
| | | | |
| Operating income (millions) | **$ 1,173** | $ 1,882 | $ 1,845 |
| Percent change | **(37.7)%** | 2.0% | 65.6% |
| Percent of sales | **27.3%** | 47.4% | 46.0% |

The Health Care segment serves markets that include medical clinics and hospitals, pharmaceuticals, dental and orthodontic practitioners, and health information systems. Products and services provided to these and other markets include medical and surgical supplies, skin health and infection prevention products, drug delivery systems, dental and orthodontic products, health information systems and anti-microbial solutions.

As discussed in Note 2, the global branded pharmaceuticals business was sold in December 2006 and January 2007.

In the fourth quarter of 2008, Health Care sales topped $1 billion, despite a nearly 7 percentage point penalty from currency translation. In local-currency terms, sales rose 4.5 percent, including 2.2 percent from acquisitions. 3M saw solid local-currency growth in the medical products area, specifically in core infection prevention and skin and wound care products. Geographically, the U.S. and Asia Pacific led sales growth. Operating income margins of 24.0 percent in the fourth quarter of 2008 were the highest in the Company, which includes the impact of $50 million in restructuring and exit activity charges that reduced operating income margins by 4.9 percentage points. This is a highly competitive

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environment where 3M s brand presence and high quality are clearly making a difference. Doctors, hospitals and other medical service providers continue to show a strong preference for 3M products.

For full-year 2008, Health Care s results were strong, with sales increasing 8.2 percent to $4.3 billion and operating income margins of 27.3 percent. As discussed further below, both 2007 and 2006 operating income results include significant gains from the sale of 3M s pharmaceuticals business in December 2006 and January 2007, negatively impacting the 2008 versus 2007 year-on-year operating income comparison. Local-currency sales were up 6.8 percent, largely organic, but also included 1.7 percent from acquisitions. In 2008, 3M closed a number of important bolt-on acquisitions in Health Care, including TOP-Service, a German orthodontic technology and services company offering a digital lingual solution; Imtec, an Oklahoma-based manufacturer of dental implants and cone beam computed tomography; and Solumed, a Quebec-based developer and marketer of leading-edge medical products designed to prevent infections in operating rooms and hospitals. Full-year 2008 sales were led by strong increases in 3M s medical, dental and orthodontics businesses. Sales grew in all geographies, led by strong gains in Asia Pacific and Latin America.

In 2007, Health Care sales were $3.968 billion. Local-currency growth was 18.3 percent (excluding divestitures), including 4.4 percentage points of growth from acquisitions and 4.5 percentage points of growth from supply agreements related to the sale of the global branded pharmaceuticals business. The sale of the pharmaceuticals business reduced Health Care sales growth by 23.7 percent. 3M provides disaggregated information on sales growth for Health Care s remaining businesses (without pharmaceuticals) further below.

The combination of the following items positively impacted total year 2007 Health Care operating income by $791 million. As discussed in Note 2, in January 2007 the Company sold its branded pharmaceuticals business in the Europe region. The operating income gain related to this sale, which is included in Health Care, totaled $781 million. In addition, as discussed in Note 4, a net operating income gain of $10 million was recorded in 2007, which primarily related to adjustments to restructuring costs incurred in the fourth quarter of 2006.

The combination of the following items positively impacted total year 2006 Health Care operating income by $673 million, primarily in the fourth quarter of 2006. As discussed in Note 2, in early December 2006, the Company sold its branded pharmaceuticals business in the Asia Pacific region, including Australia and South Africa. The Company also sold its branded pharmaceuticals business in the United States, Canada and Latin America in late December 2006. The operating income gain related to this sale, which is included in Health Care, totaled $1.074 billion. In addition, as discussed in Note 4, the Health Care segment for the year 2006 included $293 million in restructuring costs, primarily employee-related severance and benefit costs. Of the $293 million, $166 million was related to the pharmaceuticals business and $15 million related to Health Care severance and other costs. In addition, $112 million of severance and benefit costs were recorded in the fourth quarter of 2006 related to worldwide staff overhead reduction actions taken to streamline the Company s cost structure in response to the sale of 3M s branded pharmaceuticals business. Health Care also included $95 million of expensed in-process research and development costs related to the Brontes acquisition and $13 million in environmental reserves related to the pharmaceuticals business.

3M believes the following disaggregated information for 3M Health Care s remaining businesses (without pharmaceuticals) and for pharmaceuticals on a stand-alone basis provides useful information.

***Health Care Business without Pharmaceuticals:***

| | 2008 | 2007 | 2006 |
|---|---|---|---|
| Sales (millions) | **$ 4,293** | $ 3,968 | $ 3,237 |
| Sales change analysis: | | | |
| Local currency (volume and price) | **6.8%** | 18.3% | 8.5% |
| Divestitures | **(0.1)** | | |
| Translation | **1.5** | 4.3 | 0.7 |
| Total sales change | **8.2%** | 22.6% | 9.2% |
| | | | |
| Operating income (millions) | **$ 1,173** | $ 1,086 | $ 806 |
| Percent change | **8.0%** | 34.6% | (9.1)% |
| Percent of sales | **27.3%** | 27.4% | 24.9% |

The following discussion provides information on 3M Health Care s remaining businesses (without pharmaceuticals). Refer to the preceding section entitled Health Care Business for a discussion of sales change for 2008 compared to 2007. Operating income increased 8.0 percent to $1.173 billion, while operating income margins were maintained in excess of 27 percent. Operating income in 2008 included $60 million in restructuring actions and exit activity charges,

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primarily comprised of severance and related benefits, but also including $14 million in asset impairments. 2007 included $5 million in restructuring expenses, primarily severance and related benefits.

In 2007, sales growth was broad-based across all platforms, led by infection prevention solutions and skin and wound care therapy products in medical, HFA-based components (non-CFC) for drug inhalers in drug delivery, and healthcare funding and performance management solutions for the hospital market in health information systems. Geographically, Health Care (without pharmaceuticals) achieved strong growth rates in all major regions, led by Europe, the United States, and the combined Latin America and Canada area. Local-currency sales increased 18.3 percent, with acquisitions contributing 4.4 percentage points of this growth. Much of the acquisition growth came from two deals that closed in late 2006 Biotrace International, PLC, a U.K.-based provider of microbiology products, and SoftMed, a Maryland-based provider of health information software solutions. Health Care also closed five complementary acquisitions in 2007 to strengthen the portfolio and accelerate growth into the future in the medical, oral care and health information systems businesses. Sales growth also included 4.5 percentage points of growth due to supply agreements related to the sale of the global branded pharmaceuticals business. Operating income increased 34.6 percent, with an operating income margin of 27.4 percent. Operating income for 2007 included $5 million in restructuring expenses, primarily severance and related benefits. Operating income for 2006 included $95 million of expensed in-process research and development costs related to the Brontes acquisition and also included business-specific restructuring actions that totaled $15 million, primarily comprised of severance and related benefits plus asset impairments.

***Pharmaceuticals Business:***

| | 2008 | 2007 | 2006 |
|---|---|---|---|
| Sales (millions) | **$** | $ | $ 774 |
| Sales change analysis: | | | |
| Local currency (volume and price) | **N/A** | N/A | (3.5)% |
| Translation | **N/A** | N/A | 0.6 |
| Total sales change | **N/A** | N/A | (2.9)% |
| | | | |
| Operating income (millions) | **$** | $ 796 | $ 1,039 |

The combination of the following items positively impacted total year 2007 pharmaceuticals operating income by $796 million. As discussed in Note 2, in January 2007 the Company sold its branded pharmaceuticals business in the Europe region. The operating income gain related to this sale totaled $781 million. In addition, as discussed in Note 4, a net operating income gain of $15 million was recorded in 2007, which primarily related to adjustments to restructuring costs incurred in the fourth quarter of 2006. Drug Delivery Systems Division (part of Health Care without Pharmaceuticals) is a source of supply to the acquiring companies and records sales and operating income related to the pharmaceuticals supply agreements.

In total, the combination of the following items positively impacted total year 2006 pharmaceuticals operating income by $783 million, primarily in the fourth quarter of 2006. As discussed in Note 2, in early December 2006, the Company sold its branded pharmaceuticals business in the Asia Pacific region, including Australia and South Africa. The Company also sold its branded pharmaceuticals business in the United States, Canada and Latin America in late December 2006. The operating income gain related to these transactions totaled $1.074 billion. As discussed in Note 4, $112 million of severance and benefit costs were recorded in the fourth quarter of 2006 related to worldwide staff overhead reduction actions taken to streamline the Company s cost structure in response to the sale of 3M s branded pharmaceuticals business. As also discussed in Note 4, the pharmaceuticals business for total year 2006 included $97 million in employee-related severance and benefits and $69 million of asset impairments and other expenses. In addition, an environmental reserve of $13 million was recognized related to the pharmaceuticals business.

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***Safety, Security and Protection Services Business (14.4% of consolidated sales):***

| | 2008 | 2007 | 2006 |
|---|---|---|---|
| Sales (millions) | **$ 3,642** | $ 3,070 | $ 2,663 |
| Sales change analysis: | | | |
| Local currency (volume and price) | **18.3%** | 10.8% | 13.7% |
| Divestitures | **(1.7)** | | |
| Translation | **2.0** | 4.5 | 1.1 |
| Total sales change | **18.6%** | 15.3% | 14.8% |
| | | | |
| Operating income (millions) | **$ 736** | $ 611 | $ 549 |
| Percent change | **20.4%** | 11.3% | 7.1% |
| Percent of sales | **20.2%** | 19.9% | 20.6% |

The Safety, Security and Protection Services segment serves a broad range of markets that increase the safety, security and productivity of workers, facilities and systems. Major product offerings include personal protection products, safety and security products (including border and civil security solutions), energy control products, cleaning and protection products for commercial establishment s, track and trace solutions, and roofing granules for asphalt shingles. In the second quarter of 2008, 3M completed the sale of its HighJump Software business which provided supply chain execution software solutions. 3M s Track and Trace Solutions utilizes radio frequency identification (RFID) technology to provide a growing array of solutions from library patron self-checkout systems to tracking packages.

In the fourth quarter of 2008, sales in this business rose 2.9 percent to $769 million. Local-currency sales increased 13 percent, driven by 3M s 2008 acquisition of Aearo Technologies. Acquisitions contributed approximately 16 percentage points of growth in the fourth quarter. On a geographic basis, sales for the quarter were strongest in the United States, followed by the Asia Pacific region. Operating income in the fourth quarter declined 12.8 percent, which included $12 million in restructuring expenses.

Full-year 2008 sales increased 18.6 percent. In local-currency terms, sales rose approximately 18 percent, comprised of 14 points from acquisitions and 2 points each from organic volumes and selling price increases. Sales growth was led by acquisitions, primarily Aearo, along with organic growth in personal protection solutions, protective window films, and cleaning solutions for commercial buildings, and RFID solutions (Track and Trace). Aearo, acquired in April 2008, manufactures and sells personal protection and energy absorbing products. Aearo expanded 3M s platform by adding hearing protection as well as eyewear and fall protection product lines to 3M s existing line of respiratory products. In July 2008, 3M acquired Quest Technologies Inc., a manufacturer of environmental monitoring equipment, including noise, heat stress and vibration monitors. The sale of HighJump Software (discussed below) resulted in a 1.7 percentage point penalty to full-year sales. Worldwide operating income was up 20.4 percent to $736 million.

In 2008, 3M announced and completed the sale of its HighJump Software business and recognized a pre-tax loss of $23 million in the second quarter of 2008. In addition, 3M recorded restructuring charges and exit activities that totaled $15 million in 2008. Including the preceding 2008 items, operating income margins were in excess of 20 percent for 2008. In the second quarter of 2007, 3M recorded a restructuring charge of $29 million related to the phaseout of operations at its New Jersey roofing granule facility. This included fixed asset impairments and employee-related restructuring liabilities.

In 2007, local-currency sales in the Safety, Security and Protection Services segment were up 10.8 percent. Acquisitions contributed 7.4 percentage points of this growth, including a carry-over benefit from the August 2006 acquisition of Security Printing and Systems Limited. Sales growth was led by the respiratory protection business, followed by the security systems, corrosion protection and building and commercial services businesses. 2007 sales growth was held back by market softness in the U.S. residential construction market, which negatively impacted the roofing granules business. The decline in the roofing granules business reduced Safety, Security and Protection Services 2007 sales growth by approximately 1.5 percent. Geographically, sales growth was led by Europe and the combined Latin America and Canada area. This segment recorded a restructuring charge of $29 million in the second quarter of 2007 related to the phaseout of operations at its New Jersey roofing granule facility. This included fixed asset impairments and employee-related restructuring liabilities. Including this charge, operating income margins were approximately 20 percent for total year 2007. In 2006, operating income includes $10 million in restructuring expenses, primarily severance and related benefits.

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***Consumer and Office Business (13.6% of consolidated sales):***

| | 2008 | 2007 | 2006 |
|---|---|---|---|
| Sales (millions) | **$ 3,448** | $ 3,411 | $ 3,172 |
| Sales change analysis: | | | |
| Local currency (volume and price) | **(0.3)%** | 5.0% | 7.4% |
| Translation | **1.4** | 2.5 | 0.7 |
| Total sales change | **1.1%** | 7.5% | 8.1% |
| | | | |
| Operating income (millions) | **$ 663** | $ 692 | $ 633 |
| Percent change | **(4.1)%** | 9.2% | 3.4% |
| Percent of sales | **19.2%** | 20.3% | 20.0% |

The Consumer and Office segment serves markets that include consumer retail, office retail, home improvement, building maintenance and other markets. Products in this segment include office supply products, stationery products, construction and home improvement products, home care products, protective material products and consumer health care products.

In the fourth quarter of 2008, Consumer and Office sales declined 11.2 percent to $765 million. Local currency sales were down 6.5 percent and currency impacts reduced sales by just under 5 percentage points. U.S. sales declined by 13 percent, heavily impacted by the ongoing slump in U.S. consumer retail spending levels. More than 50 percent of sales in Consumer and Office are generated within the United States. By far the biggest contributor to this decline was the retail and wholesale office channel. The combination of massive office worker layoffs, coupled with across-the-board declines in office retail foot traffic, had a dramatic and negative impact on sales. 3M businesses serving other U.S. retail channels performed well in the fourth quarter despite this rough economic environment. This business posted positive local-currency sales for its home care products, such as Scotch-Brite Scrub Sponges, and for its do-it-yourself retail channel. Elsewhere around the globe, 3M s Consumer and Office business drove positive local-currency sales growth in both Latin America and Asia Pacific, but overall growth was muted by declines in Europe. Worldwide operating income declined in the fourth quarter, including the impact of $18 million in restructuring charges, which contributed 11.4 percentage points of this 35.5 percent decline.

For total year 2008, Consumer and Office sales grew just over 1 percent. This business has successfully created new products and designed new programs and planograms with their large U.S. customers in order to mitigate what is a very tough end-market situation. Sales growth was led by home care and do-it-yourself products. Operating income declined 4.1 percent and margins were in excess of 19 percent, an outstanding return considering what was a slow U.S. market environment and a synchronized slowdown in growth across most others areas of the world. Geographically, sales growth was led by Asia Pacific and Latin America. Operating income was negatively impacted by the $18 million in restructuring charges discussed in the preceding paragraph.

Going forward, 3M expects sales growth in the Consumer and Office segment to continue to be led by international operations as U.S. growth will remain uncertain over the near term due to challenging economic conditions.

In 2007, Consumer and Office experienced broad-based local-currency sales growth of 5.0 percent, led by the construction and home improvement and home cleaning businesses. In construction and home improvement, products such as Scotch-Blue Painter s Tape, Filtrete Furnace Filters and Command Mounting Products, helped drive results. Geographically, international growth led sales, while a slowdown in the United States was driven by soft overall U.S. retail sales and a soft residential housing environment. Operating income increased 9.2 percent and exceeded 20 percent of sales.

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***Display and Graphics Business (12.9% of consolidated sales):***

| | 2008 | 2007 | 2006 |
|---|---|---|---|
| Sales (millions) | **$ 3,255** | $ 3,904 | $ 3,747 |
| Sales change analysis: | | | |
| Local currency (volume and price) | **(17.9)%** | 2.7% | 5.0% |
| Divestitures | **(0.3)** | (0.4) | |
| Translation | **1.6** | 1.9 | 0.3 |
| Total sales change | **(16.6)%** | 4.2% | 5.3% |
| | | | |
| Operating income (millions) | **$ 580** | $ 1,163 | $ 1,045 |