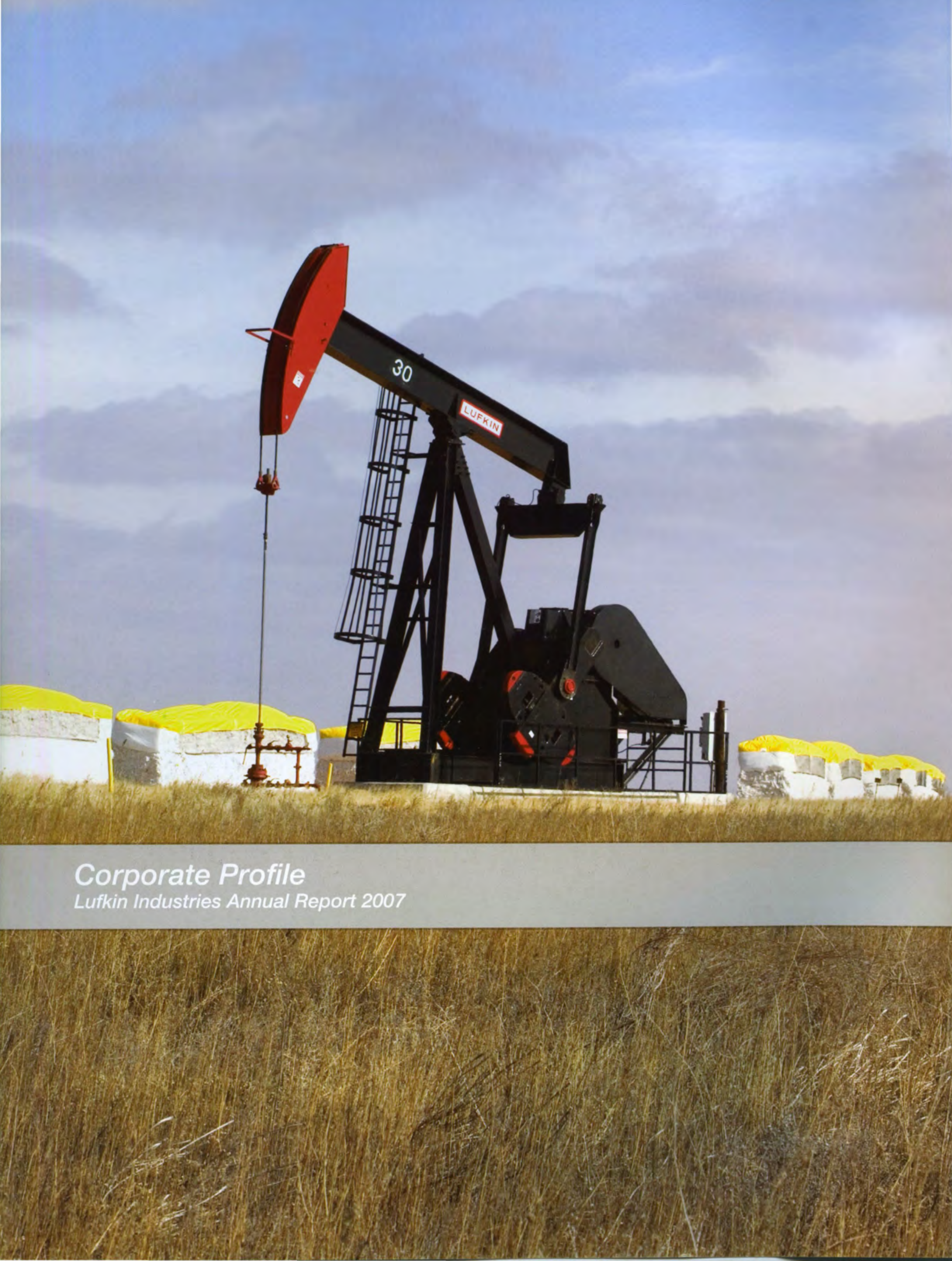
LUFKIN INDUSTRIES, INC.

2007 Annual Report

Oil Field • Power Transmission



Corporate Profile
Lufkin Industries Annual Report 2007

Oil Field Products and Services

LUFKIN IS A LEADING GLOBAL PROVIDER of artificial lift oil field equipment and services, primarily consisting of highly adaptable pumping units, automation technology equipment and a variety of services including on-site installation, technical support and maintenance. Additionally, the Company operates a gray and ductile iron foundry producing up to 300 tons per day of captive and commercial castings for the heavy equipment, valve and machine tool markets. Lufkin maintains a significant presence in all major oil markets.

Power Transmission Products and Services

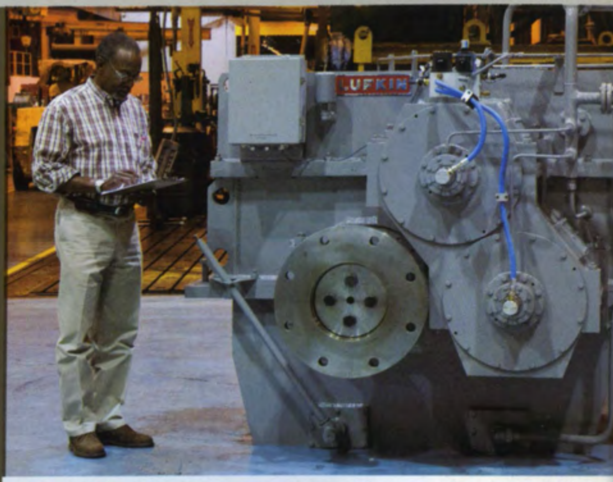
LUFKIN IS A MAJOR SUPPLIER TO THE GLOBAL power transmission equipment market. These are primarily custom, high-precision gear units ranging in power from 20 to 125,000 horsepower and above, with weights up to 250 tons. These highly-engineered products are used in a wide variety of industrial and marine applications, such as Oil and Gas, Power Generation, Refining, Marine Propulsion, Petrochemicals, Steel, Rubber, and Sugar. Lufkin's global Aftermarket and Field Service organization targets the repair and refurbishment of gear installations worldwide, while supporting the sales of new power transmission equipment.

Founded in 1902, Lufkin Industries, Inc. (Nasdaq: LUFK) is a vertically integrated company that designs, engineers, manufactures, sells, installs and services high quality and high valued-added oil field equipment and power transmission products across the globe.

Notice of Annual Meeting

Lufkin Industries Annual Report 2007

The Annual Meeting of Shareholders of Lufkin Industries, Inc. will be held at the Museum of East Texas, 503 North Second Street, Lufkin, Texas on May 7, 2008, at 9:00 a.m. local time.



This RHS2500HG marine propulsion gearbox is one of two units installed on the "Pati R. Moran" (shown above).

	December 31,				
(Thousands of dollars, except per share amounts)	**2007**	**2006**	**2005**	**2004**	**2003**
Sales	$597,187	$605,492	$492,167	$356,281	$262,255
Operating expenses	489,853	502,237	422,961	333,568	247,782
Earnings before income taxes	112,726	104,729	69,275	22,704	15,706
Net earnings	74,211	72,994	44,544	14,417	9,738
Earnings per share:					
Basic*	$4.98	$4.92	$3.10	$1.06	$0.74
Diluted*	$4.92	$4.83	$3.03	$1.04	$0.73
Dividends per share*	$0.88	$0.62	$0.38	$0.36	$0.36
Total assets	500,656	429.069	359,795	300,269	263,656
Working capital	224,733	181,957	133,628	87,231	70,831
Long-term notes payable, net of current portion	-	-	-	-	-
Shareholders' equity	384,653	328,140	261,078	208,932	188,196

* Years 2003 - 2004 adjusted for 2-for-1 Stock Split effective on April 19, 2005.

Letter to the Shareholders

Lufkin Industries Annual Report 2007

Letter to the Shareholders

Lufkin Industries produced record earnings in 2007, strongly validating the strategic initiatives we have put in place over the past several years to expand our participation in international markets. Worldwide demand remained strong for energy, as well as the products required to extract and produce that energy. This demand underlies, to a great extent, the performance of both our Power Transmission and Oil Field divisions. Decreased North American activity in the oil patch led to a softening of demand for our products in this market, but the shift to the international markets more than offset this decrease. As a result of Lufkin Industries being positioned to respond to these international opportunities, the company was able to both improve earnings during 2007, as well as increase its market share in growing markets outside of North America.

An important aspect of 2007 was the successful transition to new leadership of the company as several officers reached retirement age. Experienced managers within the company assumed most positions. Jay Glick has been elected as the new CEO of the company, bringing nearly 14 years of Lufkin experience, as well as 20 years of outside oil field related experience, to his new role. With Jay's election to President and CEO, Terry L. Orr was elected Vice President and General Manager of the company's Power Transmission division. Mr. Orr has been employed by Lufkin since August 1976, and has played a key role in the global growth of the division as the Director of Sales and Marketing for the Power Transmission division. In addition, we also introduced new, talented leadership in our Oil Field organization from outside of the company, as Mark Crews was appointed Vice President and General Manager of the Oil Field division, adding his 30 years of experience in the oil field industry to the existing, experienced management team.

Lufkin's total sales for 2007 were $597.2 million compared to $605.5 million for 2006. Power Transmission sales increased to 26.5% of total Company sales from 20.6% in 2006, while Trailer sales declined to 6.9% of the total from 13.1% the prior year, reflecting the dire state of the U.S. trailer markets. The continued decline in the market for trailer products, coupled with the depressed market price levels, led to our decision to suspend Lufkin's participation in those markets, which the company formally announced to the public in January 2008. Sales from the Oil Field division were relatively constant at 66.6% of total sales, up slightly from 66.3% in 2006. The company's backlog increased 11.8% during 2007, closing the year at $202.5 million. Power Transmission and Oil Field had combined backlog increases of 22.3%, which more than offset the drop in Trailer backlog during the year.

Each division improved its gross margin for 2007, but the change in the mix of sales between higher margin Power Transmission revenue and the decrease in Trailer's mix, which typically provides relatively lower margins, had a positive impact on consolidated profit margins, which were 27.9% of sales, up from 25.8% in 2006. The increase in consolidated gross margin resulted in an improved operating income and net earnings, even after SG&A increased to 9.9% of sales for 2007 from 8.8% for 2006. Among other factors, the increase in SG&A reflected the increased expense associated with international sales offices, travel

Douglas V. Smith
Chairman of the Board

J. F. Glick
President
Chief Executive Officer

and commissions. Due to improved profit margins, Lufkin's earnings per diluted share for 2007 grew to $4.92 from $4.83 for 2006, which included a tax benefit of $0.26 from accruals for tax credits and the van line closure. Excluding this net benefit, earnings per diluted share increased 7.7% in 2007 compared to 2006.

Lufkin's financial results for 2007 strengthened the company's year-end financial position. The cash flow from operations increased 33.9% to $90.3 million for 2007 from 2006 and funded stock repurchases of 500,000 shares for $27.5 million under our share buyback authorization, capital expenditures of $19.3 million and a 42.0% increase in our cash dividend to $13.1 million. Even with these expenditures, cash and cash equivalents increased 65.7% during 2007 to $95.7 million at year end. We had no bank debt at the end of 2007, and during the fourth quarter, we expanded our credit facility to $40.0 million from $27.5 million, while extending its maturity through 2010. Shareholders' equity increased 17.2% during 2007 to $384.7 million at year end.

Prospects for further profitable growth for 2008 are reinforced by the substantial momentum of our Power Transmission sales and international Oil Field sales for 2007, as well as the improved performance in our domestic Oil Field business in the last half of the year. Although the company is well positioned to capitalize on the opportunities the energy markets will offer in 2008, we are ever mindful of the challenges presented by the volatility inherent in those markets and cyclical economic forces that bear on them. As we demonstrated in 2007, we will maintain our ability to respond to this volatility in the short and intermediate term, while implementing our long-term strategies to strengthen our industry leadership and, thereby, drive long-term profitable growth and increased shareholder value.

Oil Field – For 2007, sales were $397.4 million for our Oil Field division, down 1.0% or $3.8 million from 2006. Demand for pumping equipment remained strong throughout the year in Latin American and Middle East markets. We also successfully increased sales into Eastern Europe during 2007.

North American bookings of oil pumping equipment declined 23.3% for 2007, although they rebounded well for the fourth quarter with an increase of 29.9% compared to the fourth quarter of 2006. In Canada, sales for the year were affected by an early and prolonged spring break-up, rising costs, volatile commodities prices and proposed revisions to both the tax structure and royalty payments in Alberta. While Canada is not a large percentage of our total company's results, it is strategically important to us and we have been active in Canada for over 60 years. Consequently, we take a longer term perspective on these issues.

We believe demand in the United States was affected by a variety of factors, beginning in the fourth quarter of 2006. Oil price volatility and heightened mergers and acquisitions activity, slowed decision making and delayed capital projects. In addition, the decline in prices for natural gas reduced demand for our smaller pumps, which are used to lift water in coal bed methane and natural gas applications. We also saw increased foreign competition in the sector that normally is supported by used equipment. In the absence of an adequate supply of used pumping units, this sector bought imported units. Lastly, as producers attempted to stay within budgets, capital earmarked for the U.S. market was diverted to international and offshore projects, which are usually larger in size but typically have longer planning horizons and are more difficult to quickly cut back. The improved demand evident in the fourth quarter supports our expectations for 2008 that demand will stabilize and improve. We will remain alert to indications of rising cost pressure in the United States as end users focus on controlling costs in an uncertain economic environment.

We expect demand for the Oil Field division's automation products and oil field services businesses to continue growing at a significant rate as end users rely more heavily on Lufkin's expertise in managing rod pumping installations and as they recognize the economic benefits of lower personnel costs, improved equipment life and increased up time that derive from automation technologies.

Continued strong demand for Lufkin's Oil Field products and services throughout the year, combined with improved North American demand for pumping equipment in the fourth quarter, drove an expanded Oil Field backlog to $76.9 million at the end of 2007, up 14.5% from the end of 2006 and 20.7% from the end of the third quarter of 2007.

Power Transmission – With bookings increasing to a new record for a fourth consecutive year, Power Transmission sales increased 26.8% to $158.5 million for 2007, and the backlog grew 27.8% to $122.2 million. Even with the increasing volume of shipments from the Power Transmission division, bookings have outpaced revenues for eight sequential quarters through the end of 2007. The growth in revenues generated stronger operating leverage, producing an increase in gross margin to 33.1% of sales for 2007 from 32.8% for 2006, despite cost increases related to expanding our manufacturing capacity during the year.

The growth in Power Transmission bookings are driven largely by the global demand for energy. The oil and gas, power generation, refining, petrochemical and marine sectors continued to fuel the demand for Lufkin's gear products. In addition, our repair and retrofit services were also in high demand, in both domestic and international markets, as companies upgraded and refurbished equipment to take advantage of improved efficiency and greater reliability. To meet this demand, manufacturing capacity was expanded in the U.S and France. Demand for our low speed gears for industrial applications also increased during 2007. The demand came chiefly from such basic industries as metals processing and mining, as these industries invested in gearing to expand their capacity and capitalize on the increasing market for their products.

Based on long-term expectations for energy demand and the expansion of the global economy, we are confident of the Power Transmission division's prospects for continued growth in 2008 and beyond. Given the capacity we have in place, coupled with expansion investments that are in process, the Power Transmission division should be well positioned to capitalize on the continued growth in demand for its products and services.

Trailer – Sales for the Trailer division were $41.4 million for 2007, a decline of 47.9% from 2006. As anticipated, sales for 2007 were affected by our decision to exit the lower margin van trailer business in the third quarter of 2006 and by difficult conditions in the construction, housing and auto industries, among other soft domestic markets. Through our decision to focus in 2007 on the production of flat bed and specialized dump trailers, the division produced an increase in its gross margin for 2007 to 11.6% from 7.3% for 2006. However, the reduction in sales lowered the division's contribution to consolidated net earnings to approximately breakeven for the year. Because of this performance and our expectations for a continuation of difficult market conditions for 2008, the Board of Directors authorized the company to suspend its participation in the commercial trailer markets it serves and to develop a plan to run-out existing inventories, fulfill current contractual obligations and close all Trailer facilities. We expect to complete this process in the first half of 2008.

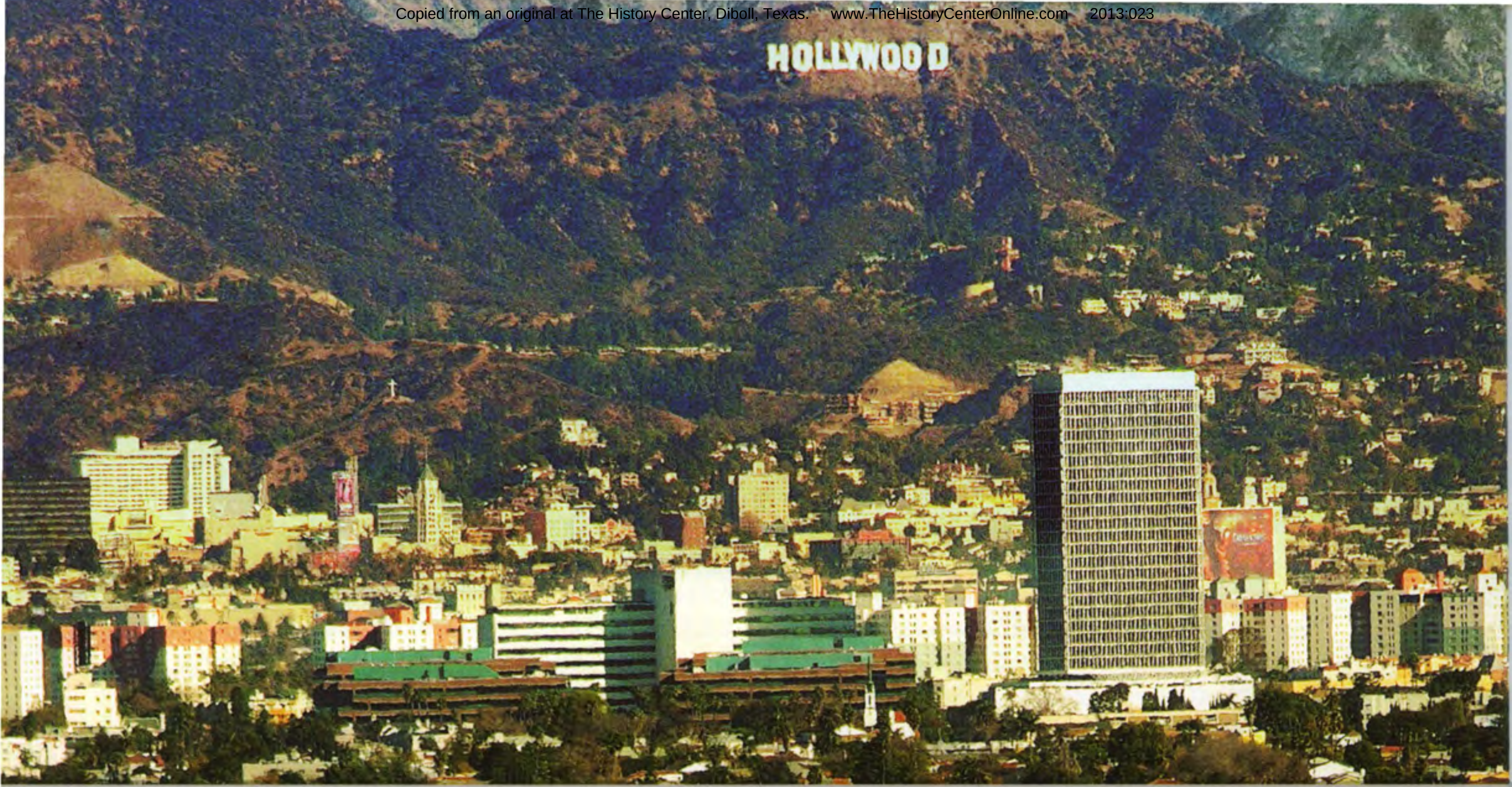
Summary – In responding to and overcoming the challenges of this past year, the people of Lufkin Industries demonstrated their skills, professionalism, and dedication to our customers and shareholders. We thank them for their hard work, past and future, and we also thank our Board of Directors for their oversight and commitment to sound business principles. In closing, we thank you, our fellow shareholders, for your investment in Lufkin Industries.

Sincerely,

Douglas V. Smith

Douglas V. Smith
Chairman of the Board

John F. "Jay" Glick
President and Chief Executive Officer



Oil Field and Power Transmissions Divisions

Lufkin Industries Annual Report 2007

OIL FIELD DIVISION

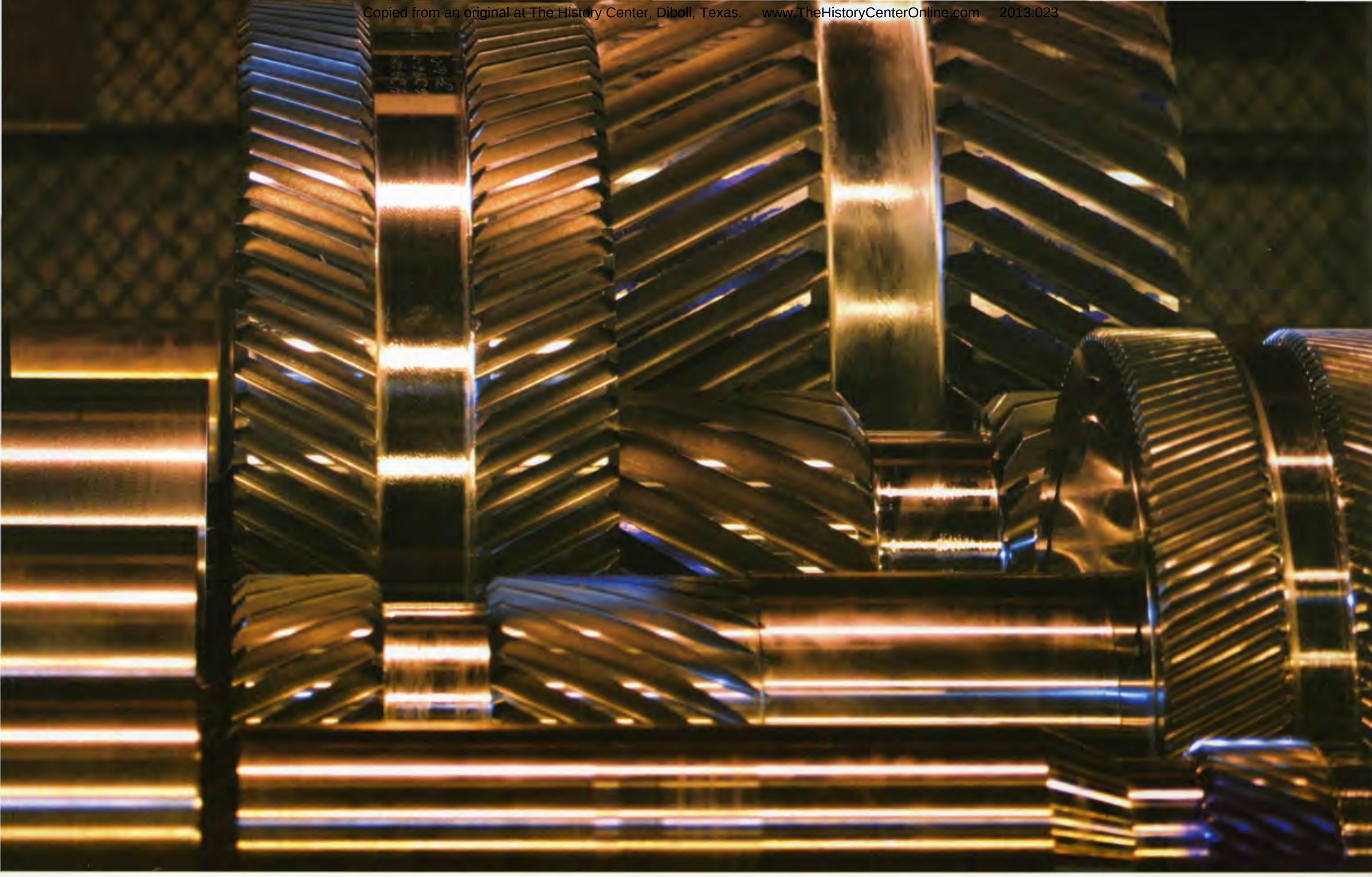
The Oil Field Division is a vertically integrated global leader in the manufacture, installation and service of artificial lift systems for oil and gas field applications. The Company commands a significant share of its markets, which include capital equipment, automation technology equipment and service. To serve these markets, Lufkin operates manufacturing facilities in three countries and has an international network of service centers, sales offices and sales representation affiliations in over 40 countries.

The Company produces a broad line of beam lift pumping units that are customized for the particular depth and producing characteristics of each well or reservoir. In addition to traditional oil well lifting applications, Lufkin pumping units are increasingly used to lift water off of producing natural gas wells to reduce downhole pressure and enhance recovery. Lufkin can provide a full artificial lift system including design, installation, and field maintenance optimized using the company's proprietary software, RODSTAR™. Pumping units are manufactured in Lufkin plants located in Texas, Canada and Argentina.

Lufkin also sells oil field automation equipment that reduces the total cost of operating and maintaining lift systems by automating the operation of the pumping units and optimizing well performance using sophisticated software and instrumentation. In addition to automating pumping units, Lufkin supplies control equipment to automate gas injection and progressive cavity pump wells. Sales of variable speed drives coupled with Lufkin rod pump controllers for heavy oil well applications grew substantially in 2007. Lufkin is a world leader in the sale of state-of-the-art rod pump automation controllers, offering systems with advanced technological features that differentiate them from other products currently in the market.

Lufkin supports its pumping unit products business with a broad-based, well trained service organization, through which the Company installs, repairs and maintains equipment in the field. The Company provides service personnel to work in-house with oil and gas producers to assist them in developing and maintaining a comprehensive system maintenance and optimization program. A natural extension of its pumping unit and automation businesses, the expansion of the Company's service capabilities has been an integral part of its strategy to be a full-service provider of integrated beam lifting systems and services. Lufkin has service centers in the U.S.A., Canada, Argentina, Oman and Egypt. These service centers install, optimize, maintain, and repair Lufkin equipment and can provide on-site support of one pumping unit or an entire fleet of units. Lufkin also maintains warehouses around the world stocked with a full compliment of OEM spare parts available to maintain maximum up-time for oil and gas producers.

As another key aspect of the Company's strategy of vertical integration, Lufkin operates a gray and ductile iron foundry capable of producing high quality castings both for captive and commercial applications. The foundry produces castings ranging in size from 100 pounds to 15 tons for pumping units as well as for external customers in the heavy equipment, valve and machine tool markets. Having dedicated foundry capacity has cemented the Company's competitive advantage by reducing lead times to a minimum for production of oil field and power transmission castings, thus enabling the Company to respond to tight customer delivery and quality requirements.



POWER TRANSMISSION DIVISION

Lufkin is one of the world's leading suppliers of mechanical power transmission products and services. The Power Transmission Division's products are highly engineered precision gear drives that are utilized in both speed increasing and speed reducing services across a wide spectrum of industrial applications. These units transmit powers that range from 20 HP to in excess of 120,000 horsepower and which weigh from as low as 300 pounds to as much as 250 tons. Lufkin provides full product engineering and manufacturing in both the US and Europe with its modern, highly-capable factories. The Division differentiates itself through its engineering excellence, superior customer service, industry-recognized product reliability, rapid delivery, and strong global after-sales support.

The Division's gear products are classed into two primary segments: high-speed turbo-machinery units and low-speed high-torque units. One of the primary markets for Lufkin's high speed turbo gears is the oil and gas sector. The gearbox is used to transfer the power from the prime mover, such as a gas turbine or an electric motor, to the driven machine, such as a centrifugal compressor or a pump. Our turbo gear products are used on land and on offshore platforms for such applications as gas compression and oil production, on pipelines for crude oil and gas transmission, and for oil refining. Other important and strategic applications are electrical power generation, marine propulsion, petrochemicals manufacture, and liquefied natural gas (LNG) production and distribution.

In all these applications, an equipment failure and the attendant down-time is disruptive and extremely costly to the user and, potentially, to the consumer. Lufkin combines its world-class expertise in engineering, metallurgy and manufacturing technology to produce equipment with a proven history of reliability, superior performance, and lengthy service life. The safety and reliability of Lufkin equipment translate into utilization and equipment-availability levels that create demonstrable value to the user and provide Lufkin with a strong competitive advantage. In addition to our product strengths, Lufkin offers the logistical advantage of design, manufacturing, and product performance testing capability in both Europe and the U.S. We are the only turbo gear manufacturer able to offer this full range of global support.

For the fourth consecutive year, the Power Transmission division delivered a record performance in both sales and order intake. Sales of $158.5 million were up 27% from $124.9 million in 2006. Even with record shipments, our new order intake of $185.1 million resulted in a year-end backlog of $122.2 million, up 28% from $95.6 million at the end of 2006.

The growth in the Division continued to be driven by strong core markets, coupled with our focus on operational excellence and our expansion of the Division's global reach. Strong energy and infrastructure markets drove the demand for our gear products. New orders from the electrical power generation increased 24% to $21.1 million, up from the 2006 level of $17 million. Lufkin gearboxes are used with both steam and gas turbines to drive electric generators. Environmental and economic concerns provide an incentive to industrial users to recover and utilize their waste heat in cogeneration applications.

The Marine Propulsion sector generated even stronger bookings growth, increasing 116% to $20.1 million vs. $9.3 million in 2006. Lufkin manufactures propulsion drives targeted for the work boat industry, which includes inland river tow boats, offshore supply vessels (OSVs), anchor handling tug and supply boats (AHTs), articulated tug and barge (ATBs), ferries and medium-size bulk and liquid-carrier ships. The rise in bulk cargo shipping via the inland rivers is driven by increasingly traffic-congested highways and higher fuel prices, while the demand for offshore work boats is necessitated by the need to support oil and gas production platforms which are operating in ever-deeper waters.

Lufkin's core product line of high speed turbo gears is used in compression, pumping, and electrical generating applications throughout the oil and gas, oil refining, and petrochemicals sectors. New orders in these segments declined somewhat from the record levels experienced in 2006, largely the result of market economics on new project starts combined with the full order books enjoyed by engineering contractors and primary OEMs. Bookings in oil and gas declined from $58 million in 2006 to $50 million in 2007. Total bookings in this segment are still at a historically high level with strong fundamentals and bright prospects for the future. Investment in this sector will continue to be driven by capacity expansions to address the growing, global demand for gasoline and by environmental requirements in both Europe and the U.S. for further reductions in the sulfur level in diesel fuels.

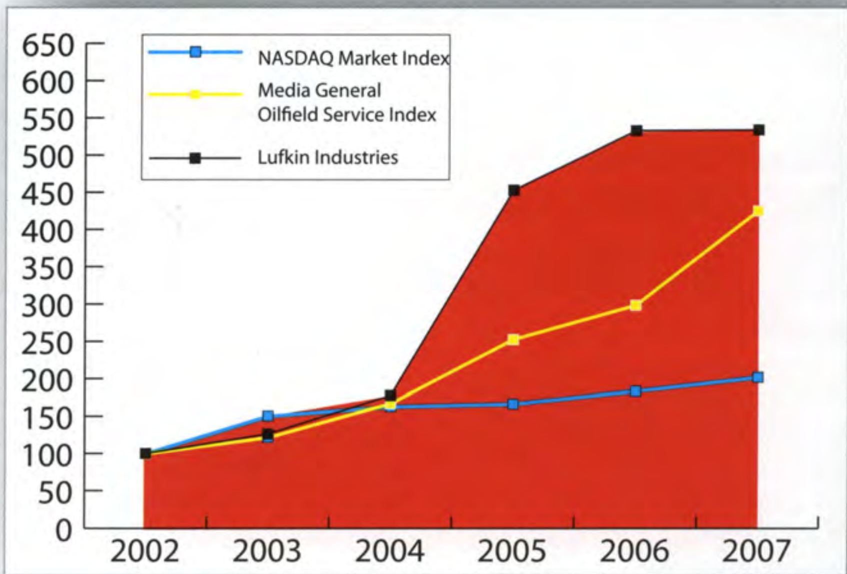
Lufkin Industries also supply low-speed gear products for mining, metals processing, and sugar processing applications. While demand from both mining and metals processing declined during 2007 from the record levels seen during 2005 and 2006, bookings from these sectors remained strong compared to historic levels.

Our strategies for continued growth of our global footprint and for expansion of our sales organization across Europe, Asia, and the Middle East continue to open new opportunities for our Power Transmission products and services. This is complemented by our manufacturing and engineering organizations that enable Lufkin Industries to offer superior products with the shortest lead times in the industry. Our unique position as the only turbo gear manufacturer with manufacturing, design and performance testing facilities in North America and Europe enables full product support in both the Eastern and Western Hemispheres. Although we believe we are well positioned for future growth, we continue to explore promising expansion opportunities for the profitable growth of our Power Transmission business.

Market Price of and Dividends on the Registrant's Common Equity and Related Stockholder Matters

The following performance graph compares the performance of the Company's common stock to the NASDAQ Market Value Index and to the Media General Oilfield Services Index (which includes the Company) for the last five years. The graph assumes that the value of the investment in the Company's common stock and each index was $100 at December 31, 2002 and reinvestment of dividends.

COMPARISON OF CUMULATIVE TOTAL RETURN OF ONE OR MORE COMPANIES, PEER GROUPS, INDUSTRY INDEXES AND/OR BROAD MARKETS



Performance Graph data provided by R. R. Donnelley Financial.

Fiscal Year Ending

	12/31/02	12/31/03	12/31/04	12/31/05	12/31/06	12/31/07
Lufkin Industries	100.00	126.26	177.82	452.80	532.83	533.83
Media General Oilfield Service Index	100.00	121.99	167.42	253.03	298.70	425.38
NASDAQ Market Index	100.00	150.36	163.00	166.58	183.68	201.91

The performance graph will not be deemed to be soliciting material under the proxy rules or incorporated by reference into any filing except to the extent that the Company specifically incorporates it.

Board Members

Lufkin Industries Annual Report 2007

Douglas V. Smith
Chairman of the Board
***Chairman** –*
Executive Committee
Board member since 1993

J. F. Glick
President
Chief Executive Officer
Board member since 2007

S. W. Henderson, III
Member –
Executive Committee
Compensation Committee
Nominating/Governance Committee
Board member since 1971

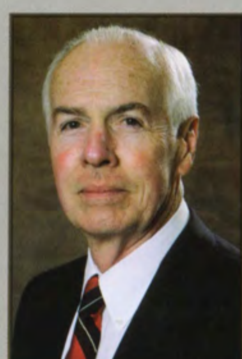
H. J. Trout, Jr.
***Chairman** –*
Pension Committee
Member –
Executive Committee
Nominating/Governance Committee
Board member since 1980

Thomas E. Wiener
Member –
Executive Committee
Pension Committee
Nominating/Governance Committee
Board member since 1987

B. H. O'Neal
***Chairman** – Compensation Committee*
Member –
Audit Committee
Nominating/Governance Committee
Board member since 1992

John H. Lollar
***Chairman** – Audit Committee*
Member –
Compensation Committee
Board member since 1997

J. T. Jongebloed
***Chairman** –Nominating/ Governance Committee*
Member –
Audit Committee
Compensation Committee
Board member since 2002



John F. Anderson
Member –
Executive Committee
Pension Committee
Board member since 2003

Suzanne V. Baer
Member –
Audit Committee
Pension Committee
Board member since 2005

Corporate Officers

J. F. Glick
President
Chief Executive Officer

M. E. Crews
Vice President,
General Manager –
Oil Field Division

T. L. Orr
Vice President,
General Manager –
Power Transmission Division

S. H. Semlinger
Vice President,
General Manager –
Manufacturing Technology

P. G. Perez
Vice President,
General Counsel
Corporate Secretary

R. D. Leslie
Vice President,
Treasurer,
Chief Financial Officer

Key Locations

Corporate Offices
P. O. Box 849
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936-634-2211

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Lufkin Automation
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281-495-1100

Foundry Sales
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936-634-2211

Oil Field Domestic Service
Headquarters/Sales
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Lufkin, TX 75902-0849
936-634-2211

Gear Repair and Service
Headquarters/Sales
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Lufkin Argentina Sales & Services
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1003 Buenos Aires, Argentina
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Lufkin Industries, Inc. –
Sales Office
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39-0587-734-472

Common Stock Transfer Agent

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Chicago, IL 60602
866-781-1368

Auditors

Deloitte & Touche, LLP
333 Clay Street, Suite 2300
Houston, TX 77002-4196
713-982-2000

Form 10-K

LUFKIN INDUSTRIES, INC.

The following is a discussion of the Company's business, financial results and financial condition. This report is part of the Company's Annual Report on Form 10-K that has been filed with the Securities and Exchange Commission. Certain parts of that filing in this report have been omitted, such as the cover page and exhibits. A complete copy of the Company's Annual Report on Form 10-K is available on the SEC's website at *www.sec.gov* or free of charge on the Company's website at *www.lufkin.com.* The Company will also provide to any shareholder a copy of that report without charge upon written request. Please mail your requests to Investor Relations, P.O. Box 849, Lufkin, Texas 75902.

PART I

Item 1. Business

Lufkin Industries, Inc. (the "Company") was incorporated under the laws of the State of Texas on March 4, 1902, and since that date has maintained its principal office and manufacturing facilities in Lufkin, Texas. The Company employed approximately 2,700 people at December 31, 2007, including approximately 1,850 that were paid on an hourly basis. Certain operations are subject to a union contract that expires in October 2008. The Company is divided into three operating segments: Oil Field, Power Transmission and Trailer.

In January 2008, the Company announced the decision to suspend its participation in the commercial trailer markets and to develop a plan to run-out existing inventories, fulfill contractual obligations and close all trailer facilities during 2008. See the Trailer section below for more information.

Oil Field

Products:
The Oil Field segment manufactures and services artificial reciprocating rod lift equipment, commonly referred to as pumping units, and related products.
Pumping Units- Four basic types of pumping units are manufactured: an air-balanced unit; a beam-balanced unit; a crank-balanced unit; and a Mark II Unitorque unit. The basic differences between the four types relate to the counterbalancing system. The depth of a well and the desired fluid production determine the type of counterbalancing configuration that is required. There are numerous sizes and combinations of Lufkin oil field pumping units within the four basic types.
Service- Through a network of service centers, the Company transports and repairs pumping units. The service centers also refurbish used pumping units.
Automation- The Company designs, manufactures, installs and services computer control equipment and analytical services for pumping units that lower production costs and optimize well efficiency.
Foundry Castings- As part of the Company's vertical integration strategy, the Oil Field segment operates an iron foundry to produce castings for new pumping units. In order to maximize utilization of this facility, castings for third parties are also produced.

Raw Materials & Labor:
Oil Field purchases a variety of raw materials in manufacturing its products. The principal raw materials are structural and plate steel, round alloy steel and iron castings from both its own foundry and third-party foundries. Casting costs are subject to change from raw material prices on scrap iron and pig iron in addition to natural gas and electricity prices. Due to the many configurations of its products and thus sizes of raw material used, Oil Field does not enter into long-term contracts for raw materials but generally does not experience shortages of raw materials. During the period of 2005 through 2007, Oil Field did not experience any significant material shortages or rapid price increases. Raw material prices are not expected to decline in the short-term nor are shortages expected. Certain materials like steel round and bearings have continued to experience price increases and longer lead times. Raw material prices may continue to increase and availability may decrease with little notice.

The nature of the products manufactured and serviced generally requires skilled labor. Oil Field's ability to increase capacity could be limited by its ability to hire and train qualified personnel. Also, the main U.S. manufacturing facilities are unionized, so any labor disruption could have a significant impact on Oil Field's ability to maintain production levels. The current labor contract expires in October 2008.

Markets:
Demand for pumping unit equipment primarily depends on the level of new onshore oil well and workover drilling activity as well as the depth and fluid conditions of that drilling. Drilling activity is driven by the available cash flow of the Company's customers as well as their long-term perceptions of the level and stability of the price of oil. The higher energy prices experienced since 2004 have increased the demand for pumping units and related service and products from higher drilling activity, activation of idle wells and the upgrading of existing wells. During 2007, demand in the North American market has been negatively affected, compared to 2006 levels, by the impact of lower natural gas prices on coal-bed methane and other unconventional gas production that use rod pumps to de-water wells, drilling program delays from M&A activity, cost control efforts deferring or reducing capital spending programs and the competitive pressure from lower-priced pumping units in areas traditionally served by the used unit market. Traditionally, as pumping unit demand increases and availability of used equipment diminishes, demand for new equipment increases, as was experienced in 2006. Increasingly in 2007, lower-priced imported pumping units have entered the North American market in place of used equipment and reduced the incremental demand for the Company's new pumping units. However, the demand for pumping units, oilfield services and automation

equipment continue to increase in international markets. While a majority of the segment's revenues are in North America, international opportunities continue to increase as new drilling increases and existing fields mature, requiring increased use of pumping units for artificial lift, especially in the South American, Russian and Middle Eastern markets. An Oilfield customer and its related subsidiaries represented 14.9%, 11.6% and 8.2% of consolidated company sales in 2007, 2006 and 2005, respectively. The loss of this customer would have a material adverse effect on this segment.

Competition:
The primary global competitor for new pumping units and automation equipment is Weatherford, but Chinese manufacturers of pumping units are increasingly present in the market. Used pumping units are also an important factor in the North American market, as customers will generally attempt to satisfy requirements through used equipment before purchasing new equipment. While the Company believes that it is one of the larger manufacturers of sucker rod pumping units in the world, manufacturers of other types of units (submersibles and hydraulics) have a significant share of the total artificial lift market. While Weatherford is the Company's single largest competitor in the service market, small independent operators provide significant competitive pressures.

Because of the competitive nature of the business and the relative age of many of the product designs, price, delivery time, product quality and customer service are important factors in winning orders. To this end, the Company maintains strategic levels of inventories in order to ensure delivery times and invests in new capital equipment to maintain quality and price levels.

Power Transmission

Products:
The Power Transmission segment designs, manufactures and services speed increasing and reducing gearboxes for industrial applications. Speed increasers convert lower speed and higher torque input to higher speed and lower torque output while speed reducers convert higher speed and lower torque input to lower speed and higher torque output. The Company produces numerous sizes and designs of gearboxes depending on the end use. While there are standard designs, the majority of gearboxes are customized for each application.
High-Speed Gearboxes- Single stage gearboxes with pitch line velocities equal to or greater than 35 meters per second or rotational speeds greater than 4500 rpm or multi-stage gearboxes with at least one stage having a pitch line velocity equal to or greater than 35 meters per second and other stages having pitch line velocities equal to or greater than 8 meters per second. These gearboxes require extremely high precision manufacturing and testing due to the stresses on the gearing. The ratio of increasers to reducers is fairly even. These gearboxes more typically service the energy related markets of petrochemicals, refineries, offshore production and transmission of oil and gas.
Low-Speed Gearboxes- Gearboxes which do not meet the pitch line or rotational speed criteria of high-speed gearboxes are classified as low-speed gearboxes. The majority of low-speed gearboxes are reducers. While still requiring close tolerances, these gearboxes do not require the same precision of manufacturing and testing. These gearboxes more typically service commodity-related industries like rubber, sugar, paper, steel, plastics, mining and cement as well as marine propulsion.
Parts- The Company manufactures capital spares for customers in conjunction with the production of new gearboxes, as well as producing parts for aftermarket service.
Repair & Service- The Company provides on and off-site repair and service for not only its own products but also those manufactured by other companies. Repair work is performed in dedicated facilities due to the high turn-around times required.

Raw Materials & Labor:
Power Transmission purchases a variety of raw materials in manufacturing its products. The principal raw materials are steel plate, round alloy steel, iron castings and steel forgings. Due to the customized nature of its products, Power Transmission generally does not enter into long-term contracts for raw materials. Though raw material shortages are infrequent, lead times can be long due to the custom nature of many of its orders. Raw material prices are not expected to decline in the short-term and may continue to increase with little notice. Certain materials like steel round and bearings have continued to experience price increases and longer lead times. Raw material and component part shortages are not expected in the short-term, but certain supplier lead-times have grown, especially bearing suppliers.

The nature of the products manufactured and serviced generally requires skilled labor. Power Transmission's ability to increase capacity could be limited by its ability to hire and train qualified personnel. Also, the main U.S. manufacturing facilities are unionized, so any labor disruption could have a significant impact on Power Transmission's ability to maintain production levels. The current labor contract expires in October 2008.

Markets:
Power Transmission services many diverse markets, with high-speed gearing for markets such as petrochemicals, refineries, offshore production and transmission of oil and low-speed gearing for the gas, rubber, sugar, paper, steel, plastics, mining, cement and marine propulsion, each of which has its own unique set of drivers. Favorable conditions for one market may be unfavorable for another market. Generally, if general global industrial capacity utilizations are not high, spending on new equipment lags. Also impacting demand are government regulations involving safety and environmental issues that can require capital spending. Recent market demand increases have come from energy-related markets such as refining, petrochemical, drilling, coal, marine and power generation in response to higher global energy prices. These market trends are expected to continue throughout 2008, assuming energy prices stay at or near recent levels.

Competition:
Despite the highly technical nature of the products in this segment, there are many competitors. While several North American competitors have de-emphasized the market, many European companies remain in the market. Competitors include Flender Graffenstaden, BHS, Renk, Kreiter GearTech, Rientjes, Falk, and Horsburgh & Scott. While price is an important factor, proven designs, workmanship and engineering support are critical factors. Due to this, the Company outsources very little of the design and manufacturing processes.

Trailer

Products:
The Trailer segment manufactures various highway trailers for the freight-hauling market.
Vans- General-purpose dry-freight vans. Historically these have been the highest production trailer in the segment. However, due to van trailer manufacturing over-capacity and the entry of additional competitors, van trailer pricing reached a level that did not yield acceptable returns on the capital employed. In the third quarter of 2006, the Company announced its decision not to accept additional orders for new van trailers. After the existing backlog of van trailers was manufactured by early 2007, the van trailer manufacturing capacity was redeployed for additional flatbed and dump production.
Flatbeds- Flatbed style trailers used in hauling heavier loads that do not require protection from outdoor elements.
Dumps- Trailers designed to haul bulk materials like gravel or sand.
Parts- Through a network of company-owned branches, both trailers produced by the Company and by others are supported by replacement parts.

Raw Materials & Labor:
Trailer purchases a variety of raw materials in manufacturing its products. The principal raw materials are aluminum, structural and plate steel, axles, suspensions, tires, plywood and hardwood flooring. Trailer had annual contracts for aluminum for van production in order to mitigate price fluctuations, but due to the configurable nature of its products, Trailer does not have long-term purchase contracts on its other raw material purchases. Raw material shortages have been infrequent. Raw material prices are not expected to decline in the short-term nor are shortages expected.

The nature of the products manufactured generally requires skilled labor. Trailer's ability to increase capacity could be limited by its ability to hire and train qualified personnel. Also, the main U.S. manufacturing facilities are unionized, so any labor disruption could have a significant impact on Trailer's ability to maintain production levels. The current labor contract expires in October 2008.

Markets:
The Company primarily sells its trailer products in the United States to small and medium size fleet freight-hauling companies through a dealer network. Demand in this market is driven by the available cash flow or financing capabilities of the industry, age of the trailer fleets, changes in government regulations, availability of quality used trailers and the medium-term outlook for freight volumes. The profitability of the freight-hauling market is driven by freight volumes, fuel prices, wage levels and insurance costs. Due to poor market conditions, the Company decided in the third quarter of 2006 not to participate in the van market until market conditions support better operating margins. This decision gave Trailer the capability to expand manufacturing capacity of flatbed and dump trailers quickly in response to market demand. However, recent flatbed and dump trailer demand has decreased due to the reduced activity in the home and road construction markets as well as reduced profitability from higher fuel prices. In 2007, industry order rates and backlog for flatbed trailers decreased over 40% and for dump trailers over 25% compared to 2006 levels. In the fourth quarter of 2007, industry order rates and backlog for flatbed and dump trailers decreased almost 50% compared to the fourth quarter of 2006. Due to these market conditions, in January 2008, the Company announced the decision to suspend its participation in the commercial trailer markets and to develop a plan to run-out existing inventories, fulfill contractual obligations and close all trailer facilities during 2008.

Competition:
The trailer market is highly competitive with relatively low barriers to entry. The majority of the cost of a new trailer comes from purchased materials of aluminum, steel, tires, axles and wood flooring. Since there is minimal product differentiation in this market, price is the key driver. The companies with the highest market share are Great Dane and Wabash, along with several other large manufacturers like Utility, Stoughton, Fontaine, Vanguard and Hyundai. The Company does not have a significant market share in the trailer market.

See Note 16 in Notes to Consolidated Financial Statements included in this report for financial information about the Company's business segments and geographic areas.

Federal Regulation and Environmental Matters

The Company's operations are subject to various federal, state and local laws and regulations, including those related to air emissions, wastewater discharges, the handling of solid and hazardous wastes and occupational safety and health. Environmental laws have, in recent years, become more stringent and have generally sought to impose greater liability on a larger number of potentially responsible parties. While the Company is not currently aware of any situation involving an environmental claim that would likely have a material adverse effect on its business, it is always possible that an environmental claim with respect to one or more of the Company's current businesses or a business or property that one of our predecessors owned or used could arise that could have a material adverse effect. The Company's operations have incurred, and will continue to incur, capital and operating expenditures and other costs in complying with these laws and regulations in both the United States and abroad. However, the Company does not anticipate the future costs of environmental compliance will have a material adverse effect on its business, financial results or results of operations.

Available Information

The Company makes available, free of charge, through our website, www.lufkin.com, its annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, as soon as reasonably practicable after it electronically files such material with, or furnishes such material to, the Securities and Exchange Commission.

Item 1A. Risk Factors.

The risks described below are those which the Company believes are the material risks that it faces. Any of the risk factors described below could significantly and adversely affect its business, prospects, financial condition and results of operations.

A decline in domestic and worldwide oil and gas drilling activity would adversely affect the Company's results of operations.

The Oil Field segment is materially dependent on the level of oil and gas drilling activity in North America and worldwide, which in turn depends on the level of capital spending by major, independent and state-owned exploration and production companies. This capital spending is driven by current prices for oil and gas and the perceived stability and sustainability of those prices. Oil and gas prices have been subject to significant fluctuation in recent years in response to changes in the supply and demand for oil and gas, market uncertainty, world events, governmental actions, and a variety of additional factors that are beyond the Company's control, including:

- the level of North American and worldwide oil and gas exploration and production activity;
- worldwide economic conditions, particularly economic conditions in North America;
- oil and gas production costs;
- weather conditions;
- the expected costs of developing new reserves;
- national government political requirements and the policies of OPEC;
- the price and availability of alternative fuels;
- the effect of worldwide energy conservation measures;
- environmental regulation; and
- tax policies.

The business of the Trailer segment is highly cyclical, which could adversely affect its business and results of operations.

The truck trailer manufacturing industry historically has been and is expected to continue to be cyclical, as well as affected by overall economic conditions. New trailer production for the trailer industry reached its most recent peak of approximately 306,000 units in 1999, falling to approximately 140,000 by 2001, rebounding to approximately 280,000 units in 2006 and falling to approximately 217,000 in 2007. Customers historically have replaced trailers in cycles that run from five to 12 years, depending on service and trailer type. Poor economic conditions can adversely affect demand for new trailers and in the past have led to an overall aging of trailer fleets beyond this typical replacement cycle. Due to poor market conditions, the Company decided in the third quarter of 2006 not to participate in the van market, and, in January 2008, announced the decision to suspend participation in the commercial trailer markets and to develop a plan to run-out existing inventories, fulfill contractual obligations and close all trailer facilities in 2008.

Increases in the prices of our raw materials could adversely affect our margins and results of operations.

The Company uses large amounts of steel, iron and electricity in the manufacture of its products. The price of these raw materials has a significant impact on the cost of producing products. Steel and electricity prices have increased significantly in the last five years, caused primarily by higher energy prices and increased global demand. Since most of the Company's suppliers are not currently parties to long-term contracts with us, the Company is vulnerable to fluctuations in prices of such raw materials. Factors such as supply and demand, freight costs and transportation availability, inventory levels of brokers and dealers, the level of imports and general economic conditions may affect the price of cast iron and steel. Raw material prices may increase significantly in the future. Certain items such as steel round, bearings and aluminum have continued to experience price increases, price volatility and longer lead times. If the Company is unable to pass future raw material price increases on to its customers, margins, results of operations, cash flow and financial condition could be adversely affected.

Interruption in our supply of raw materials could adversely affect our results of operations.

The Company relies on various suppliers to supply the components utilized to manufacture our products. The availability of the raw materials is not only a function of the availability of steel and iron, but also the alloy materials that are utilized by our suppliers. To date, these shortages have not caused a material disruption in availability or our manufacturing operations. However, material disruptions may occur in the future. Raw material shortages and allocations may result in inefficient operations and a build-up of inventory, which can negatively affect the Company's working capital position. The loss of any of the Company's suppliers or their inability to meet its price, quality, quantity and delivery requirements could have an adverse effect on the Company's business and results of operations.

The inherent dangers and complexity of the Company's operations could subject it to substantial liability claims that could adversely affect our results of operations.

The products that the Company manufactures and the services that it provides are complex, and the failure of this equipment to operate properly or to meet specifications may greatly increase our customers' costs. In addition, many of these products are used in inherently hazardous industries, such as the oil and gas drilling and production industry where an accident or product failure can cause personal injury or loss of life, damage to property, equipment, or the environment, regulatory investigations and penalties and the suspension of the end-user's operations. If the Company's products or services fail to meet specifications or are involved in accidents or failures, we could face warranty, contract, or other litigation claims for which it may be held responsible and its reputation for providing quality products may suffer.

The Company's insurance may not be adequate in risk coverage or policy limits to cover all losses or liabilities that we may incur or be responsible. Moreover, in the future we may not be able to maintain insurance at levels of risk coverage or policy limits that we deem adequate or at premiums that are reasonable for us, particularly in the recent environment of significant insurance premium increases. Further, any claims made under the Company's policies will likely cause its premiums to increase.

Any future damages deemed to be caused by the Company's products or services that are assessed against it and that are not covered by insurance, or that are in excess of policy limits or subject to substantial deductibles, could have a material adverse effect on our results of operations and financial condition. Litigation and claims for which we are not insured can occur, including employee claims, intellectual property claims, breach of contract claims, and warranty claims.

We may not be able to successfully integrate future acquisitions, which will cause us to fail to realize expected returns.

The Company continually explores opportunities to acquire related businesses, some of which could be material to the Company. The ability to continue to grow, however, may depend upon identifying and successfully acquiring attractive companies, effectively integrating these companies, achieving cost efficiencies and managing these businesses as part of the Company. The Company may not be able to effectively integrate the acquired companies and successfully implement appropriate operational, financial and management systems and controls to achieve the benefits expected to result from these acquisitions. The Company's efforts to integrate these businesses could be affected by a number of factors beyond its control, such as regulatory developments, general economic conditions and increased competition. In addition, the process of integrating these businesses could cause the interruption of, or loss of momentum in, the activities of our existing business. The diversion of management's attention and any delays or difficulties encountered in connection with the integration of these businesses could negatively impact the Company's business and results of operations. Further, the benefits that the Company anticipates from these acquisitions may not develop.

Labor disputes, increasing labor costs and the expiration of our current labor contract could have a material adverse effect on our business.

The Company's main U.S. manufacturing facilities are unionized and the current labor contract with respect to those facilities expires in October 2008. The Company cannot assure that any disputes, work stoppages or strikes will not arise in the future. In 2002, a strike involving union employees, which continued for approximately 14 consecutive days, resulted in operating losses for us. In addition, when our existing collective bargaining agreement expires, the Company cannot assure that it will be able to reach a new agreement with its employees or that any new agreement will be on substantially similar terms as the existing agreement. Labor costs may increase significantly as a result of the negotiations for any new labor agreement. Future disputes with and labor concessions to the Company's employees could have a material adverse effect upon its results of operations and financial position.

The inability to hire and retain qualified employees may hinder our growth.

The ability to provide high-quality products and services depends in part on the Company's ability to hire and retain skilled personnel in the areas of management, product engineering, servicing and sales. Competition for such personnel is intense and competitors can be expected to attempt to hire the Company's skilled employees from time to time. In particular, the Company's business and results of operations could be materially adversely affected if it is unable to retain the customer relationships and technical expertise provided by the Company's management team and professional personnel.

Significant competition in the industries in which the Company operates may result in its competitors offering new or better products and services or lower prices, which could result in a loss of customers and a decrease in revenues.

The industries in which the Company operates are highly competitive. The Company competes with other manufacturers and service providers of varying sizes, some of which may have greater financial and technological resources than it does. As an example, barriers to entry in the standard truck trailer manufacturing industry are low. As a result, it is possible that additional competitors could enter the trailer market at any time. In the recent past, the manufacturing over-capacity and high leverage of some of our competitors in the trailer industry, along with the bankruptcies and financial stresses that affected the industry, contributed to significant pricing pressures. This pricing pressure led to the Company's decision in 2006 not to accept additional orders for van trailers. In January 2008, the Company announced the decision to suspend its participation in the commercial trailer markets and to develop a plan to run-out existing inventories, fulfill contractual obligations and close all trailer facilities.

If the Company is unable to compete successfully with other manufacturers and service providers, it could lose customers and its revenues may decline. In addition, competitive pressures in the industry may affect the market prices of the Company's new and used equipment, which, in turn, may adversely affect its sales margins, results of operations, cash flow and financial condition.

Disruption of our manufacturing operations or management information systems would have an adverse effect on our financial condition and results of operations.

While the Company owns numerous facilities domestically and internationally, its primary manufacturing facilities in and around Lufkin, Texas accounts for a significant percentage of its manufacturing output. An unexpected disruption in the Company's production at these facilities or in its management information systems for any length of time would have an adverse effect on our business, financial condition and results of operations.

The Company has foreign operations that would be adversely impacted in the event of war, political disruption, civil disturbance, economic and legal sanctions and changes in global trade policies.

The Company has operations in certain international areas, including parts of the Middle East and South America, that are subject to risks of war, political disruption, civil disturbance, economic and legal sanctions (such as restrictions against countries that the U.S. government may deem to sponsor terrorism) and changes in global trade policies. The Company's operations may be restricted or prohibited in any country in which these risks occur. In particular, the occurrence of any of these risks could result in the following events, which in turn, could materially and adversely impact the Company's results of operations:

- disruption of oil and natural gas exploration and production activities;
- restriction of the movement and exchange of funds;
- inhibition of our ability to collect receivables;
- enactment of additional or stricter U.S. government or international sanctions; and
- limitation of our access to markets for periods of time.

Results of operations could be adversely affected by actions under U.S. trade laws.

Although the Company is a U.S.-based manufacturing and services company, it does own and operate international manufacturing operations that support its U.S.-based business. If actions under U.S. trade laws were instituted that limited the Company's access to these products, the ability to meet its customer specifications and delivery requirements would be reduced. Any adverse effects on the Company's ability to import products from its foreign subsidiaries could have a material adverse effect on our results of operations.

The Company is subject to currency exchange rate risk, which could adversely affect its results of operations.

The Company is subject to currency exchange rate risk with debt denominated in U.S. dollars owed to its U.S. entity by its Canadian subsidiary. The Company cannot assure that future currency exchange rate fluctuations will not have an adverse affect on its results of operations.

Significant changes in pension fund investment performance or assumptions relating to pension costs may have a material effect on the valuation of pension obligations, the funded status of pension plans, and our pension cost.

Our funding policy for our pension plan is to accumulate plan assets that, over the long-run, will approximate the present value of projected benefit obligations. Our pension cost is materially affected by the discount rate used to measure pension obligations, the level of plan assets available to fund those obligations at the measurement date and the expected long-term rate of return on plan assets. Our pension plan is supported by pension fund investments that are volatile and subject to financial market risk, including fixed income, domestic and foreign equity securities, real estate and hedge funds. Significant changes in investment performance or a change in the portfolio mix of invested assets could result in corresponding increases and decreases in the valuation of plan assets or in a change of the expected rate of return on plan assets. A change in the discount rate would result in a significant increase or decrease in the valuation of pension obligations, affecting the reported funded status of our pension plans as well as the net periodic pension cost in the following fiscal years. Similarly, changes in the expected return on plan assets could result in significant changes in the net periodic pension cost for subsequent fiscal years.

The Company's common stock has experienced, and may continue to experience, price volatility.

The trading price of the Company's common stock has been and may continue to be subject to large fluctuations. The Company's common stock price may increase or decrease in response to a number of events and factors, including:

- trends in the Company's industries and the markets in which it operates;
- changes in the market price of the products the Company sells;
- the introduction of new technologies or products by the Company or its competitors;
- changes in expectations as to the Company's future financial performance, including financial estimates by securities analysts and investors;
- operating results that vary from the expectations of securities analysts and investors;
- announcements by the Company or its competitors of significant contracts, acquisitions, strategic partnerships, joint ventures, financings or capital commitments;
- changes in laws and regulations; and
- general economic and competitive conditions.

Item 1B. Unresolved Staff Comments.

None

Item 2. Properties

The Company's major manufacturing facilities are located in and near Lufkin, Texas, are company-owned and include approximately 150 acres, a foundry, machine shops, structural shops, assembly shops and warehouses. The facilities by segment are:

Oilfield:	
Pumping Unit Manufacturing	240,000 sq. ft.
Foundry Operations	687,000 sq. ft.
Power Transmission:	
New Unit Manufacturing	458,000 sq. ft.
Repair Operations	84,000 sq. ft.
Trailer Manufacturing	388,000 sq. ft.
Corporate Facilities	33,000 sq. ft.

Also, the Company has numerous service centers throughout the U.S. to support the Oil Field, Power Transmission and Trailer segments. The majority of these locations are company-owned, with some leased. None of these leases qualify as capital leases.

Item 2. Properties (continued)

Internationally, there are company-owned facilities for the production and servicing of pumping units and power transmission products. The facilities by segment are:

Oilfield (Pumping unit manufacturing and repair):	
Nisku, Alberta, Canada	66,000 sq. ft.
Comodoro Rivadia, Argentina	125,000 sq. ft.

Power Transmission (New unit manufacturing and repair):	
Fougerolles, France	377,000 sq. ft.

Also, the Company has several international service centers to support the Oil Field segment. The majority of these locations are owned by the Company, with some leased. None of these leases qualify as capital leases.

Item 3. Legal Proceedings

A class action complaint was filed in the U.S. District Court for the Eastern District of Texas on March 7, 1997, by an employee and a former employee who alleged race discrimination in employment. Certification hearings were conducted in Beaumont, Texas in February 1998 and in Lufkin, Texas in August 1998. In April 1999, the District Court issued a decision that certified a class for this case, which included all black employees employed by the Company from March 6, 1994, to the present. The case was closed from 2001 to 2003 while the parties unsuccessfully attempted mediation. Trial for this case began in December 2003, but was postponed by the District Court and was completed in October 2004. The only claims made at trial were those of discrimination in initial assignments and promotions.

On January 13, 2005, the District Court entered its decision finding that the Company discriminated against African-American employees in initial assignments and promotions. The District Court also concluded that the discrimination resulted in a shortfall in income for those employees and ordered that the Company pay those employees back pay to remedy such shortfall, together with pre-judgment interest in the amount of 5%. On August 29, 2005, the District Court determined that the backpay award for the class of affected employees would be $3.4 million (including interest to January 1, 2005) and provided a formula for attorney fees that the Company estimates will result in a total not to exceed $2.5 million. In addition to back pay with interest, the District Court (i) enjoined and ordered the Company to cease and desist all racially biased assignment and promotion practices and (ii) ordered the Company to pay court costs and expenses.

The Company has reviewed this decision with its outside counsel and on September 19, 2005, appealed the decision to the U.S. Court of Appeals for the Fifth Circuit. On April 3, 2007, the Company appeared before the appellate court in New Orleans for oral argument in this case. The three justices in this case will now prepare their decision and the Company believes that after a full and fair review of the evidence, the Court of Appeals will determine that the plaintiffs have not established their claims of discrimination by the Company against the plaintiffs and will enter a decision to that effect and will dismiss the case against the Company. At this time, the Company has concluded that an unfavorable ultimate outcome is not probable. If the District Court's decision is reversed and remanded for a new trial, the Company will vigorously defend itself on retrial. While the ultimate outcome and impact of these claims against the Company cannot be predicted with certainty, the Company believes that the resolutions of these proceedings will not have a material adverse effect on its consolidated financial position. However, should the Company be unsuccessful in its appeal, the final determination could have a material impact on the Company's reported earnings, results of operations and cash flows in a future reporting period.

There are various other claims and legal proceedings arising in the ordinary course of business pending against or involving the Company wherein monetary damages are sought. It is management's opinion that the Company's liability, if any, under such claims or proceedings would not materially affect its consolidated financial position, results of operations or cash flow.

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

None

PART II

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

Common Stock Information

The Company's common stock is traded on the NASDAQ Stock Market (National Market) under the symbol "LUFK." As of January 31, 2008, there were approximately 431 record holders of its common stock. This number does not include any beneficial owners for whom shares of common stock may be held in "nominee" or "street" name. The following table sets forth, for each quarterly period during fiscal 2007 and 2006, the high and low sales price per share of the Company's common stock and the dividends paid per share on the Company's common stock.

	2007			2006		
	Stock Price			Stock Price		
Quarter	High	Low	Dividend	High	Low	Dividend
First	$ 63.07	$ 50.23	$ 0.21	$ 68.67	$ 45.56	$ 0.11
Second	67.43	55.81	0.21	71.47	50.21	0.15
Third	73.25	50.73	0.23	65.21	49.05	0.18
Fourth	62.90	50.84	0.23	61.46	50.66	0.18

The Company has paid cash dividends for 68 consecutive years. Total dividend payments were $13.1 million, $9.2 million and $5.5 million in 2007, 2006 and 2005, respectively.

Equity Compensation Plan Information

The following table sets forth securities of the Company authorized for issuance under equity compensation plans at December 31, 2007.

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
Equity compensation plans approved by security holders	659,143	$30.87	1,158,868
Equity compensation plans not approved by security holders	-	-	-
Total	659,143	$30.87	1,158,868

2,200,000 shares were authorized for issuance pursuant to the 1990 Stock Option Plan, 300,000 shares were authorized for issuance pursuant to the 1996 Nonemployee Director Stock Option Plan and 2,800,000 shares were authorized for issuance pursuant to the Incentive Stock Compensation Plan 2000. In May 2007, shareholders approved the addition of 1,000,000 shares to the 2000 plan. Awards may be granted pursuant to the Incentive Stock Compensation Plan 2000 include options, restricted stock, performance awards, phantom shares, bonus shares and other stock-based awards.

Purchases of Equity Securities by the Issuer and Affiliated Purchasers

During the fourth quarter of 2007, the Company repurchased shares pursuant to a plan approved by the Board of Directors in the third quarter of 2007, under which the Company was authorized to spend up to an aggregate of $30.0 million for repurchases of its common stock. Repurchased shares are added to treasury stock and are available for general corporate purposes including the funding of the Company's stock option plans. During the fourth quarter of 2007, 100,000 shares were repurchased under the above plan at an aggregate price of $5.5 million, or an average price of $54.61. As of December 31, 2007, 500,000 shares had been repurchased at an aggregate price of $25.4 million, or $54.91 per share under the 2007 plan. As of December 31, 2007, the Company held 895,278 shares of treasury stock at an aggregate cost of approximately $31.6 million. At December 31, 2007, approximately $4.6 million of repurchase authorizations remained under the 2007 plan.

A summary of the Company's repurchase activity for the three months ended December 31, 2007, is as follows:

Issuers Purchases of Equity Securities

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans	Approximate Dollar Value of Shares That May Yet Be Purchased Under the Plans
October 1 - October 31	-	$ -	-	$ 10,084,369
November 1- November 30	-	-	-	10,084,369
December 1 - December 31	100,000	54.61	100,000	4,623,918
Total	100,000	$ 54.61	100,000	$ 4,623,918

As of December 31, 2007, 500,000 shares had been repurchased at an aggregate price of $25.4 million, or $54.91 per share under the 2007 plan. As of December 31, 2007, the Company held 895,278 shares of treasury stock at an aggregate cost of approximately $31.6 million. At December 31, 2007, approximately $4.6 million of repurchase authorizations remained under the 2007 plan.

Item 6. Selected Financial Data

Five Year Summary of Selected Consolidated Financial Data

The following table sets forth certain selected historical consolidated financial data and should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the Consolidated Financial Statements and Notes thereto included elsewhere in this annual report on Form 10-K. The following information may not be indicative of future operating results.

(In millions, except per share data)	2007	2006	2005	2004	2003
Sales	$ 597.2	$ 605.5	$ 492.2	$ 356.3	$ 262.3
Net earnings	74.2	73.0	44.5	14.4	9.7
Net earnings per share:					
Basic	4.98	4.92	3.10	1.06	0.74
Diluted	4.92	4.83	3.03	1.04	0.73
Total assets	500.7	429.1	359.8	300.3	263.7
Cash dividends per share	0.88	0.62	0.38	0.36	0.36

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

Overview

General

Lufkin Industries is a global supplier of oil field, power transmission and trailer products. Through its Oil Field segment, the Company manufactures and services artificial reciprocating rod lift equipment and related products, which are used to extract crude oil and other fluids from wells. Through its Power Transmission segment, the Company manufactures and services high-speed and low-speed speed increasing and reducing gearboxes for industrial applications. Through its Trailer segment, the Company manufactures various highway trailers, including flatbed and dump trailers. While these markets are price-competitive, technological and quality differences can provide product differentiation.

The Company's strategy is to differentiate its products through additional value-added capabilities. Examples of these capabilities are high-quality engineering, customized designs, rapid manufacturing response to demand through plant capacity, inventory and vertical integration, superior quality and customer service, and an international network of service locations. In addition, the Company's strategy is to maintain a low debt-to-equity ratio in order to quickly take advantage of growth opportunities and pay dividends even during unfavorable business cycles.

In support of the above strategy, the Company has been making capital investments in Oil Field to increase manufacturing capacity and capabilities in its three main manufacturing facilities in Lufkin, Texas, Canada and Argentina. These investments should reduce production lead times and improve quality. Investments also continue to be made to expand the Company's presence in automation products and international service, as with the recently opened service facility in Oman. In Power Transmission, the Company continues to expand its gear repair network by opening and expanding facilities in various locations in the U.S. and Canada. The Company is making targeted capital investments in the U.S. and France to expand capacity and reduce manufacturing lead times as well as certain capital investments targeting cost reductions. In Trailer, due to poor current and forecasted market conditions, in January 2008, the Company announced the decision to suspend its participation in the commercial trailer markets and to develop a plan to run-out existing inventories, fulfill contractual obligations and close all trailer facilities during 2008.

Trends/Outlook

Oilfield
Demand for pumping unit equipment primarily depends on the level of new onshore oil well and workover drilling activity as well as the depth and fluid conditions of that drilling. Drilling activity is driven by the available cash flow of the Company's customers as well as their long-term perceptions of the level and stability of the price of oil. The higher energy prices experienced since 2004 have increased the demand for pumping units and related service and products from higher drilling activity, activation of idle wells and the upgrading of existing wells. During 2007, demand in the North American market has been negatively affected, compared to 2006 levels, by the impact of lower natural gas prices on coal-bed methane and other unconventional gas production that use rod pumps to de-water wells, drilling program delays from M&A activity, cost control efforts deferring or reducing capital spending programs and the competitive pressure from lower-priced pumping units in areas traditionally served by the used unit market. Traditionally, as pumping unit demand increases and availability of used equipment diminishes, demand for new equipment increases, as was experienced in 2006. Increasingly in 2007, lower-priced imported pumping units have entered the North American market in place of used equipment and reduced the incremental demand for the Company's new pumping units. However, the demand for pumping units, oilfield services and automation equipment continue to increase in international markets. While a majority of the segment's revenues are in North America, international opportunities continue to increase as new drilling increases and existing fields mature, requiring increased use of pumping units for artificial lift, especially in the South American, Russian and Middle Eastern markets.

Power Transmission
Power Transmission services many diverse markets, with high-speed gearing for markets such as petrochemicals, refineries, offshore production and transmission of oil and slow-speed gearing for the gas, rubber, sugar, paper, steel, plastics, mining, cement and marine propulsion, each of which has its own unique set of drivers. Favorable conditions for one market may be unfavorable for another market. Generally, if general global industrial capacity utilizations are not high, spending on new equipment lags. Also impacting demand are government regulations involving safety and environmental issues that can require capital spending. Recent market demand increases have come from energy-related markets such as refining, petrochemical, drilling, coal, marine and power generation in response to higher global energy prices. These market trends are expected to continue throughout 2008, assuming energy prices stay at recent levels.

Trailer

The Company primarily sells its trailer products in the United States to small and medium size fleet freight-hauling companies through a dealer network. Demand in this market is driven by the available cash flow or financing capabilities of the industry, age of the trailer fleets, changes in government regulations, availability of quality used trailers and the medium-term outlook for freight volumes. The profitability of the freight-hauling market is driven by freight volumes, fuel prices, wage levels and insurance costs. Due to poor market conditions, the Company decided in the third quarter of 2006 not to participate in the van market until market conditions support better operating margins. Recent flatbed and dump trailer demand has decreased due to the reduced activity in the home and road construction markets as well as reduced profitability from higher fuel prices. In 2007, industry order rates and backlog for flatbed trailers decreased over 40% and for dump trailers over 25% compared to comparable 2006 levels. In the fourth quarter of 2007, industry order rates and backlog for flatbed and dump trailers decreased almost 50% compared to comparable 2006 levels. Projected market conditions for 2008 do not indicate significant improvement over current market levels, which would cause Trailer to yield unacceptable returns in these future periods. Due to these market conditions, in January 2008, the Company announced the decision to suspend its participation in the commercial trailer markets and to develop a plan to run-out existing inventories, fulfill contractual obligations and close all trailer facilities in 2008.

Summary of Results

The Company generally monitors its performance through analysis of sales, gross margin (gross profit as a percentage of sales) and net earnings, as well as debt/equity levels, short-term debt levels, and cash balances.

Overall, sales for the year ended December 31, 2007, decreased to $597.2 million from $605.5 million for the year ended December 31, 2006, or 1.4%. Sales for 2005 were $492.2 million. This decline in 2007 was primarily driven by decreased sales of van trailers related to the decision in 2006 to cease production of that product line. Additional segment data on sales is provided later in this section.

Gross margin for the year ended December 31, 2007, increased to 27.9% from 25.8% for the year ended December 31, 2006, and 23.0% for year ended December 31, 2005. This overall gross margin improvement from 2006 was primarily due to the favorable mix effect of decreased lower-margin trailer sales being offset by increased sales of higher-margin power transmission products. The gross margin improvement in 2006 over 2005 was primarily related to certain cost reductions related to capital expenditures and improved margins in Power Transmission due to increased sales of higher-margin energy-related high-speed units. Additional segment data on gross margin is provided later in this section.

The improvement in gross margin in 2007 was offset by higher selling, general and administrative expenses and a higher net tax rate. The net tax rate in 2006 was 30.3% due to the benefits of research and experimentation tax credits, current and deferred state tax rate adjustments and other estimate revisions. The Company reported net earnings of $74.2 million or $4.92 per share (diluted) for the year ended December 31, 2007, compared to net earnings of $73.0 million or $4.83 per share (diluted) for the year ended December 31, 2006. Net income of $44.5 million or $3.03 per share (diluted) was reported for the year ended December 31, 2005.

Debt/equity (long-term debt net of current portion as a percentage of total equity) levels were 0.0% as of December 31, 2007, December 31, 2006 and December 31, 2005. Cash balances at December 31, 2007, were $95.7 million, up from $57.8 million at December 31, 2006, due to higher net earnings and lower capital expenditures offsetting increased treasury stock purchases and higher dividends.

Year Ended December 31, 2007 Compared to Year Ended December 31, 2006:

The following table summarizes the Company's sales and gross profit by operating segment (in thousands of dollars):

Year Ended December 31	2007	2006	Increase/ (Decrease)	% Increase/ (Decrease)
Sales				
Oil Field	$ 397,354	$ 401,200	$ (3,846)	(1.0)
Power Transmission	158,452	124,922	33,530	26.8
Trailer	41,381	79,370	(37,989)	(47.9)
Total	$ 597,187	$ 605,492	$ (8,305)	(1.4)
Gross Profit				
Oil Field	$ 109,091	$ 109,414	$ (323)	(0.3)
Power Transmission	52,476	41,024	11,452	27.9
Trailer	4,801	5,811	(1,010)	(17.4)
Total	$ 166,368	$ 156,249	$ 10,119	6.5

Oil Field

Oil Field sales decreased slightly to $397.4 million, or 1.0%, for the year ended December 31, 2007, from $401.2 million for the year ended December 31, 2006. Increased sales of oil field services, automation equipment and new pumping units in the Middle East and Argentina markets was offset by lower sales of new pumping units in the North American market. Oil Field's backlog increased to $76.9 million as of December 31, 2007, from $67.1 million at December 31, 2006. This increase is related to increased orders for the Argentina and Middle East markets, partially offset by weaker demand for new pumping units in the North American market.

Gross margin (gross profit as a percentage of sales) for the Oil Field segment increased slightly to 27.5% for the year ended December 31, 2007, compared to 27.3% for the year ended December 31, 2006, or 0.2 percentage points.

Direct selling, general and administrative expenses for Oil Field increased to $17.5 million, or 12.1%, for the year ended December 31, 2007, from $15.6 million for the year ended December 31, 2006. This increase is due to higher employee-related expenses in support of increased sales levels. Direct selling, general and administrative expenses as a percentage of sales also increased to 4.4% for the year ended December 31, 2007, from 3.9% for the year ended December 31, 2006.

Power Transmission

Sales for the Company's Power Transmission segment increased to $158.5 million, or 26.8%, for the year ended December 31, 2007, compared to $124.9 million for the year ended December 31, 2006. This growth was the result of increased sales of high-speed units to the energy-related markets, such as power generation and oil and gas drilling, production and refining from both the U.S. and France manufacturing facilities and low-speed marine units for the coastal, river and inland-waterway transportation market. Power Transmission backlog at December 31, 2007, increased to $122.2 million from $95.6 million at December 31, 2006, primarily from sales of new units for the marine and oil-drilling markets.

Gross margin for the Power Transmission segment increased to 33.1% for the year ended December 31, 2007, compared to 32.8% for the year ended December 31, 2006, from increased plant efficiencies and fixed cost coverage from higher production volumes and the benefit of greater sales of high-speed units.

Direct selling, general and administrative expenses for Power Transmission increased to $18.3 million, or 17.4%, for the year ended December 31, 2007, from $15.6 million for the year ended December 31, 2006. This increase is due to higher employee-related expenses in support of increased sales volumes. Direct selling, general and administrative expenses as a percentage of sales, however, decreased to 11.6% for the year ended December 31, 2007, from 12.5% for the year ended December 31, 2006.

Trailer

Trailer sales for the year ended December 31, 2007, decreased to $41.4 million, or 47.9%, from $79.4 million for the year ended December 31, 2006. This decrease is primarily related to the decline in new van trailer sales, representing over 78% of the sales decline. New van sales were impacted by the Company's decision in 2006 not to take additional orders for van trailers due to poor market conditions. Sales for flatbed and dump trailers were also lower due to weakness in the home construction market, low demand in the road construction market and reduced Gulf Coast clean-up efforts from lower hurricane activity. Backlog for the Trailer segment decreased to $3.4 million at December 31, 2007, compared to $18.4 million at December 31, 2006. The backlog decrease was primarily from lower flatbed and dump orders as well as from lower van trailer backlog related to the decision to not take additional van trailer orders.

Trailer gross margin increased to 11.6% for the year ended December 31, 2007, from 7.3% for the year ended September 30, 2006, or 4.3 percentage points. This increase was primarily due to the favorable mix effect of lower van trailer sales, which traditionally had lower gross margins than flatbed or dump trailers, being partially offset by plant reconfiguration costs in the first quarter of 2007 and lower plant utilization impacting fixed cost coverage.

Direct selling, general and administrative expenses for Trailer decreased to $1.6 million, or 34.6%, for the year ended December 31, 2007, from $2.4 million for the year ended December 31, 2006, from lower general liability legal and claims expenses. Direct selling, general and administrative expenses as a percentage of sales increased to 3.9% for the year ended December 31, 2007, from 3.1% for the year ended December 31, 2006.

Corporate/Other

Corporate administrative expenses, which are allocated to the segments primarily based on historical third-party revenues, increased to $21.6 million, or 11.8%, for the year ended December 31, 2007, from $19.3 million for the year ended December 31, 2006, primarily from the higher employee-related expenses and stock option expenses.

Net interest income, interest expense and other income and expense for the year ended December 31, 2007, totaled $5.4 million of income compared to income of $1.5 million for the year ended December 31, 2006, primarily due to an increase in interest income from higher cash balances and the favorable impact of the stronger Canadian currency on U.S. dollar-denominated liabilities.

Pension income, which is reported as a reduction of cost of sales, increased to $3.3 million for the year ended December 31, 2007, or 12%, compared to $2.9 million for the year ended December 31, 2006, primarily from expected asset returns exceeding expected expense increases.

The net tax rate for the year ended December 31, 2007, was 34.2% compared to 30.3% for the year ended December 31, 2006. The lower net tax rate in 2006 was the result of several items. A tax initiative to claim research and experimentation tax credits for the 2002 through 2005 tax years and the recent legislation passed to allow a research and experimentation tax credit for the 2006 tax year produced a significant benefit to the tax rate. A lower effective state tax rate, and the related benefit to deferred tax balances, combined with the favorable impact on state deferred tax balances due to the new Texas margin tax also produced a benefit to the net tax rate. Other items such as lower international tax rates and revisions to prior period estimates produced additional benefits to the net tax rate.

Year Ended December 31, 2006 Compared to Year Ended December 31, 2005:

The following table summarizes the Company's sales and gross profit by operating segment (in thousands of dollars):

Year Ended December 31	2006	2005	Increase/ (Decrease)	% Increase/ (Decrease)
Sales				
Oil Field	$ 401,200	$ 307,075	$ 94,125	30.7
Power Transmission	124,922	106,616	18,306	17.2
Trailer	79,370	78,476	894	1.1
Total	$ 605,492	$ 492,167	$ 113,325	23.0
Gross Profit				
Oil Field	$ 109,414	$ 76,578	$ 32,836	42.9
Power Transmission	41,024	32,300	8,724	27.0
Trailer	5,811	4,463	1,348	30.2
Total	$ 156,249	$ 113,341	$ 42,908	37.9

Oil Field

Oil Field sales increased to $401.2 million, or 30.7%, for the year ended December 31, 2006, from $307.1 million for the year ended December 31, 2005. The benefit of the stronger Canadian dollar in 2006 and new service centers contributed 1.3 percentage points of this increase. Increased sales of new pumping units accounted for a majority of the balance of the increase of 29.3 percentage points. Sales of new pumping units and related service, increased from higher drilling and production primarily in the North America and Middle East markets. Also, sales of automation equipment continued to increase due to market share growth from new product offerings. Sales growth also was impacted from price increases instituted throughout 2005 in response to dramatic raw material price increases experienced in 2004 in addition to price increases instituted in 2006. Oil Field's backlog remained at $67.1 million as of December 31, 2006, from $67.5 million at December 31, 2005. Despite higher sales volumes, backlog levels have not increased due to a targeted effort to reduce lead times through higher manufacturing capacity.

Gross margin (gross profit as a percentage of sales) for the Oil Field segment increased to 27.3% for year ended December 31, 2006, compared to 24.9% for the year ended December 31, 2005, or 2.4 percentage points. Gross margins benefited from certain cost reduction related to capital expenditures and the full-year impact of price increases instituted in 2005. This margin improvement was partially offset by employee training and other expansion-related costs associated with manufacturing facility expansions in the U.S., Canada and Argentina and higher inbound freight costs.

Direct selling, general and administrative expenses for Oil Field increased to $15.6 million, or 30.5%, for the year ended December 31, 2006, from $12.0 million for the year ended December 31, 2005. This increase is due to higher employee-related expenses in support of increased current and expected sales volumes, third-party commissions and the impact of expensing stock options. Direct selling, general and administrative expenses as a percentage of sales remained at 3.9% for the year ended December 31, 2006, compared to 3.9% for the year ended December 31, 2005.

Power Transmission

Sales for the Company's Power Transmission segment increased to $124.9 million, or 17.2%, for the year ended December 31, 2006, compared to $106.6 million for the year ended December 31, 2005. This growth was the result of increased sales of high-speed units to the energy-related markets, such as power generation and oil and gas production and refining, and from the new gear repair facilities. Power Transmission backlog at December 31, 2006, increased to $95.6 million from $53.4 million at December 31, 2005, primarily from sales of new units for the energy-related markets.

Gross margin for the Power Transmission segment increased to 31.9% for the year ended December 31, 2006, compared to 31.5% for the year ended December 31, 2005, from the benefit of price increases and from increased sales of higher-margin high-speed units, partially offset by higher manufacturing overhead costs.

Direct selling, general and administrative expenses for Power Transmission increased to $15.6 million, or 15.5%, for the year ended December 31, 2006, from $13.5 million for the year ended December 31, 2005. This increase is due to higher employee-related expenses in support of increased sales volumes and the impact of expensing stock options. However, direct selling, general and administrative expenses as a percentage of sales decreased to 12.5% for the year ended December 31, 2006, from 12.7% for the year ended December 31, 2005, from leverage on higher sales volumes.

Trailer

Trailer sales for the year ended December 31, 2006, increased to $79.4 million, or 1.1%, from $78.5 million for the year ended December 31, 2005. Higher sales of new flatbed and dump trailers was offset by lower sales of new van trailers and used trailers. Sales growth in flatbed and dump trailers was strong due to the introduction of new models and demand from the home and road construction market. New van sales were impacted by the Company not booking lower margin orders as competitors have lowered prices in response to industry manufacturing overcapacity and trucking industry issues such as soft freight demand and driver shortages. In light of current conditions in the trailer van market, the Company has declined to take additional orders for van trailers in order to expand manufacturing capacity for the production of flatbed and dump trailers and will be converting part of the Trailer factory to the production of oil field equipment. Backlog for the Trailer segment decreased to $18.4 million at December 31, 2006, compared to $25.5 million at December 31, 2005. The backlog decrease was primarily from lower van trailer backlog related to the decision to not take additional van trailer orders, partially offset by increased orders for new flatbed trailers, as described above.

Trailer gross margin increased to 7.3% for the year ended December 31, 2006, from 5.7% for the year ended December 31, 2005, or 1.6 percentage points. This included the impact of the van-related equipment and inventory expenses, which reduced margins by approximately a 1.2 percentage points. This increase was due to higher selling prices for, and the favorable mix impact of, higher-margin flatbed and dump trailers, partially offset by increases in aluminum costs for van trailers and plant inefficiencies from flatbed and dump trailer production ramp-up.

Direct selling, general and administrative expenses for Trailer decreased to $2.4 million, or 12.3%, for the year ended December 31, 2006, from $2.8 million for the year ended December 31, 2005. In 2005, bad debt expense was increased due to a disputed receivable. This also caused direct selling, general and administrative expenses as a percentage of sales to decrease to 3.1% for the year ended December 31, 2006, from 3.6% for the year ended December 31, 2005.

Corporate/Other

Corporate administrative expenses, which are allocated to the segments primarily based on historical third-party revenues, increased to $19.3 million, or 21.9%, for the year ended December 31, 2006, from $15.9 million for the year ended December 31, 2005, primarily from the impact of expensing stock options and higher employee-related expenses.

Interest income, interest expense and other income and expense for the year ended December 31, 2006, totaled $1.5 million of income compared to income of $0.1 million for the year ended December 31, 2005, primarily due to an increase in interest income from higher cash balances.

Pension income, which is reported as a reduction of cost of sales, increased to $2.9 million for the year ended December 31, 2006, or 37%, compared to $2.1 million for the year ended December 31, 2005. This increase is primarily due to higher expected returns from increased asset balances. Pension income in 2007 is expected to increase slightly to $3.2 million.

The net tax rate for the year ended December 31, 2006, was 30.3% compared to 35.7% in the year ended December 31, 2005. This lower net tax rate was the result of several items. A tax initiative to claim research and experimentation tax credits for the 2002 through 2005 tax years and the recent legislation passed to allow a research and experimentation tax credit for the 2006 tax year produced a significant benefit to the tax rate. A lower effective state tax rate, and the related benefit to deferred tax balances, combined with the favorable impact on state deferred tax balances due to the new Texas margin tax also produced a benefit to the net tax rate. Other items such as the lower international tax rates and revisions to prior period estimates produced additional benefits to the net tax rate.

Liquidity and Capital Resources

The Company has historically relied on cash flows from operations and third-party borrowing to finance its operations, including acquisitions, dividend payments and stock repurchases. The Company believes that its cash flows from operations and its available borrowing capacity under its credit agreements will be sufficient to fund its operations, including planned capital expenditures, dividend payments and stock repurchases, through December 31, 2008, and the foreseeable future.

The Company's cash balance totaled $95.7 million at December 31, 2007, compared to $57.8 million at December 31, 2006. For the year ended December 31, 2007, net cash provided by operating activities was $90.3 million, net cash used in investing activities totaled $18.1 million, net cash used in financing activities amounted to $34.1 million and the unfavorable effect of foreign currency translation was $0.2 million. Significant components of cash provided by operating activities included net earnings, adjusted for non-cash expenses, of $89.8 million and an increase in working capital of $3.8 million. This working capital increase was primarily due to higher inventory balances, which used $7.5 million, primarily from increased Power Transmission inventory related to higher sales volumes compared to the prior year. Net cash used in investing activities included net capital expenditures totaling $17.9 million. Capital expenditures in 2007 were primarily for the expansion of manufacturing capacity and efficiency improvements in the Oil Field and Power Transmission segments. Capital expenditures for 2008 are projected to be approximately $50.0 to $53.0 million, primarily for the expansion of manufacturing capacity and efficiency improvements in the Oil Field and Power Transmission segments and will be funded by operating cash flows. Significant components of net cash used by financing activities included the repurchase of common stock of $27.5 million and dividend payments of $13.1 million, or $0.88 per share, partially offset by the impact of stock option exercises, including the excess tax benefit from actual gains on stock option exercises, of $6.5 million.

The Company has a three-year credit facility with a domestic bank (the "Bank Facility") consisting of an unsecured revolving line of credit that provides up to $40.0 million of aggregate borrowing. This Bank Facility expires on December 31, 2010. Borrowings under the Bank Facility bear interest, at the Company's option, at either the greater of (i) the prime rate, (ii) the base CD rate plus an applicable margin or (iii) the Federal Funds Effective Rate plus an applicable margin or the London Interbank Offered Rate plus an applicable margin, depending on certain ratios as defined in the Bank Facility. As of December 31, 2007, no debt was outstanding under the Bank Facility. The Company was in compliance with all financial covenants under the terms of the Bank Facility. Deducting outstanding letters of credit of $7.1 million, $32.9 million of borrowing capacity was available at December 31, 2007.

During 2007, the Company repurchased shares pursuant to several plans approved by the Board of Directors, under which the Company was authorized to spend up to an aggregate of $35.0 million for repurchases of its common stock, including (1) an authorization of $3.0 million made in the third quarter of 1999, (2) an authorization of $2.0 million made in the second quarter of 2003 and (3) an authorization of $30.0 million made in the third quarter of 2007. Repurchased shares are added to treasury stock and are available for general corporate purposes including the funding of the Company's stock option plans. During 2007, 500,000 shares were repurchased under the above plans at an aggregate price of $27.5 million, or an average price of $54.99. As of December 31, 2007, 284,678 shares had been repurchased at an aggregate price of $3.0 million, or $10.54 per share under the 1999 plan, 35,817 shares had been repurchased at an aggregate price of $2.0 million, or $55.84 per share under the 2003 plan and 462,131 shares had been repurchased at an aggregate price of $25.4 million, or $54.91 per share under the 2007 plan. During the fourth quarter of 2007, 100,000 shares were repurchased at an aggregate price of approximately $5.5 million, or $54.61 per share under the 2007 plan. As of December 31, 2007, the Company held 895,278 shares of treasury stock at an aggregate cost of approximately $31.6 million. At December 31, 2007, approximately $4.6 million of repurchase authorizations remained under the 2007 plan. While this repurchase authorization has no expiration date, the Company expects to spend this remaining authorization in 2008.

The following table summarizes the Company's expected cash outflows from financial contracts and commitments as of December 31, 2007. Information on recurring purchases of materials for use in manufacturing and service operations has not been included. These amounts are not long-term in nature (less than three months) and are generally consistent from year to year.

(In thousands of dollars)

Contractual obligations	Total	Payments due by period Less than 1 year	1 - 3 years	3 - 5 years	More than 5 years
Operating lease obligations	$ 3,020	$ 1,118	$ 1,261	$ 440	$ 201
Contractual commitments for capital expenditures	10,936	10,414	522	-	-
Total	$ 13,956	$ 11,532	$ 1,783	$ 440	$ 201

Since the Company has no significant tax loss carryforwards, the Company expects to make quarterly estimated tax payments in 2008 based on taxable income levels. Also, the Company has various qualified retirement plans for which the Company has committed a certain level of benefit. The Company expects to make contributions to its pension plans of approximately $0.3 million and to its post-retirement health and life plans of approximately $0.6 million in 2008, depending on participation levels in these plans.

As discussed in Note 6 of the Consolidated Financial Statements, included in the Lufkin Consolidated Balance Sheet at December 31, 2007 is approximately $2.7 million of liabilities associated with uncertain tax positions in the jurisdictions in which Lufkin conducts business. Due to the uncertain and complex application of tax regulations, combined with the difficulty in predicting when tax audits throughout the world may be concluded, Lufkin cannot make reliable estimates of the timing of cash outflows relating to these liabilities.

Recently Issued Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 157 "Fair Value Measurements" ("SFAS 157"). SFAS 157 defines fair value, establishes a framework for measuring fair value in GAAP and expands disclosures about fair value measurements. Prior to SFAS 157, there were different definitions of fair value and limited and dispersed guidance for applying those definitions. SFAS 157 retains the exchange price notion of fair value and clarifies that the exchange price is the price in an orderly transaction between market participants to sell the asset or transfer the liability in the market in which the reporting entity would transact for the asset or liability. SFAS 157 emphasizes that fair value is a market-based measurement, not an entity-specific measurement and establishes a fair value hierarchy that distinguishes between market participant assumptions developed based on market data obtained from independent sources and the reporting entity's own assumptions. SFAS 157 also clarifies that market participant assumptions should include assumptions about risk and the effect of a restriction on the sale or use of an asset. SFAS 157 expands disclosures about the use of fair value to measure assets and liabilities in interim and annual periods and the inputs used to measure fair value. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The provisions of SFAS 157 should be applied prospectively as of the beginning of the fiscal year in which it is initially applied except for certain types of financial instruments. In February 2008, the Financial Accounting Standards Board issued FASB Staff Position ("FSP") No. FAS 157-1 and No. FAS 157-2, which delays the effective date of SFAS 157 for all nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually), to fiscal years beginning after November 15, 2008, and interim periods within those fiscal years, and removes certain leasing transactions from the scope of SFAS 157. The Company is currently evaluating the impact, if any, the adoption of SFAS 157 will have on the fair value measurement of certain investments in its qualified pension plan, but does not expect any significant impact on its consolidated financial position or results of operations.

In December 2007, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 141 (revised 2007) "Business Combinations" ("SFAS 141R"), replacing Statement of Financial Accounting Standards No. 141 "Business Combinations" ("SFAS 141"). SFAS 141R broadens the scope of SFAS 141 by applying the acquisition method of accounting to all transactions and other events in which one entity obtains control over one or businesses and not just business combinations in which control was obtained by transferring consideration. SFAS 141R also modifies the application of the acquisition method. SFAS 141R requires acquired assets and liabilities to be measured at fair value at the acquisition date versus the cost-allocation process used under SFAS 141. This change will require acquisition-related costs and restructuring costs that are expected but not legally obligated to be recognized separately from the acquisition. SFAS 141R also provides revised guidance on accounting for step acquisitions, assets and liabilities arising from contingencies, measuring goodwill and gains from bargain purchases and contingent consideration at the acquisition date. SFAS 141R applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008.

In December 2007, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 160 "Noncontrolling Interests in Consolidated Financial Statements" ("SFAS 160"). SFAS 160 amends ARB 51 and clarifies that a noncontrolling interest in a subsidiary is an ownership interest in the consolidated entity that should be reported as equity in the consolidated financial statements. SFAS 160 also modifies the income statement presentation of noncontrolling interests, establishes methods of accounting for changes in ownership interests and requires expanded disclosures of noncontrolling interests. SFAS 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008, and is to be applied prospectively as of the beginning of the fiscal year in which SFAS 160 is initially applied, except for the presentation and disclosure requirements which are retrospective for all periods. The Company does not expect the adoption of SFAS 160 to have a significant impact on its consolidated financial position or results of operations.

Management believes the impact of other recently issued standards, which are not yet effective, will not have a material impact on the Company's consolidated financial statements upon adoption.

Critical Accounting Policies and Estimates

The discussion and analysis of financial condition and results of operations are based upon the Company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses and related disclosure of contingent assets and liabilities. The Company evaluates its estimates on an ongoing basis, based on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. The Company believes the following critical accounting policies affect its more significant judgments and estimates used in preparation of its consolidated statements.

The Company extends credit to customers in the normal course of business. Management performs ongoing credit evaluations of our customers and adjusts credit limits based upon payment history and the customer's current credit worthiness. An allowance for doubtful accounts has been established to provide for estimated losses on receivable collections. The balance of this allowance is determined by regular reviews of outstanding receivables and historical experience. As the financial condition of customers change, circumstances develop or additional information becomes available, adjustments to the allowance for doubtful accounts may be required.

Revenue is not recognized until it is realized or realizable and earned. The criteria to meet this guideline are: persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the price to the buyer is fixed or determinable and collectibility is reasonably assured. In some cases, a customer is not able to take delivery of a completed product and requests that the Company store the product for a defined period of time. The Company will process a Bill-and-Hold invoice and recognize revenue at the time of the storage request if all of the following criteria are

- The customer has accepted title and risk of loss;
- The customer has provided a written purchase order for the product;
- The customer, not the Company, requested the product to be stored and to be invoiced under a Bill-and-Hold arrangement. The customer must also provide the business purpose for the storage request;
- The customer must provide a storage period and future shipping date;
- The Company must not have retained any future performance obligations on the product;
- The Company must segregate the stored product and not make it available to use on other orders; and
- The product must be completed and ready for shipment.

met:

The Company has made significant investments in inventory to service its customers. On a routine basis, the Company uses estimates in determining the level of reserves required to state inventory at the lower of cost or market. Management's estimates are primarily influenced by market activity levels, production requirements, the physical condition of products and technological innovation. Changes in any of these factors may result in adjustments to the carrying value of inventory. Also, the Company accounts for a significant portion of its inventory under the LIFO method. The LIFO reserve can be impacted by changes in the LIFO layers and by inflation index adjustments. Generally, annual increases in the inflation rate or the FIFO value of inventory cause the value of the LIFO reserve to increase.

Long-lived assets held and used by the Company are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The Company assesses the recoverability of long-lived assets by determining whether the carrying value can be recovered through projected undiscounted cash flows, based on expected future operating results. Future adverse market conditions or poor operating results could result in the inability to recover the current carrying value and thereby possibly requiring an impairment charge in the future.

Goodwill acquired in connection with business combinations represent the excess of consideration over the fair value of net assets acquired. The Company performs impairment tests on the carrying value of goodwill at least annually or whenever events or changes in circumstances indicate the carrying value of goodwill may be greater than fair value, such as significant underperformance relative to historical or projected operating results and significant negative industry or economic trends. The Company's fair value is primarily determined using discounted cash flows, which requires management to make judgments about future operating results, working capital requirements and capital spending levels. Changes in cash flow assumptions or other factors which negatively impact the fair value of the operations would influence the evaluation and may result in a determination that goodwill is impaired and a corresponding impairment charge.

The Company adopted FIN 48, *Accounting for Uncertainty in Income Taxes—an interpretation of FASB Statement No. 109*, on January 1, 2007. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in accordance with SFAS No. 109, *Accounting for Income Taxes,* by prescribing a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The application of income tax law is inherently complex. The Company is required to determine if an income tax position meets the criteria of more-likely-than-not to be realized based on the merits of the position under tax laws, in order to recognize an income tax benefit. This requires the Company to make many assumptions and judgments regarding merits of income tax positions and the application of income tax law. Additionally, if a tax position meets the recognition criteria of more-likely-than-not the Company is required to make judgments and assumptions to measure the amount of the tax benefits to recognize based on the probability of the amount of tax benefits that would be realized if the tax position was challenged by the taxing authorities. Interpretations and guidance surrounding income tax laws and regulations change over time. As a consequence, changes in assumptions and judgments can materially affect amounts recognized in the consolidated financial statements.

Deferred tax assets and liabilities are recognized for the differences between the book basis and tax basis of the net assets of the Company. In providing for deferred taxes, management considers current tax regulations, estimates of future taxable income and available tax planning strategies. Changes in state, federal and foreign tax laws as well as changes in the financial position of the Company could also affect the carrying value of deferred tax assets and liabilities. If management estimates that some or all of any deferred tax assets will expire before realization or that the future deductibility is more-likely-than-not, a valuation allowance would be recorded.

The Company is subject to claims and legal actions in the ordinary course of business. The Company maintains insurance coverage for various aspects of its businesses and operations. The Company retains a portion of the insured losses that occur through the use of deductibles. Management regularly reviews estimates of reported and unreported insured and non-insured claims and legal actions and provides for losses through reserves. As circumstances develop and additional information becomes available, adjustments to loss reserves may be required.

The Company sells certain of its products to customers with a product warranty that provides repairs at no cost to the customer or the issuance of credit to the customer. The length of the warranty term depends on the product being sold, but ranges from one year to five years. The Company accrues its estimated exposure to warranty claims based upon historical warranty claim costs as a percentage of sales multiplied by prior sales still under warranty at the end of any period. Management reviews these estimates on a regular basis and adjusts the warranty provisions as actual experience differs from historical estimates or other information becomes available.

The Company offers defined benefit plans and other benefits upon the retirement of its employees. Assets and liabilities associated with these benefits are calculated by third-party actuaries under the rules provided by various accounting standards, with certain estimates provided by management. These estimates include the discount rate, expected rate of return of assets and the rate of increase of compensation and health claims. On a regular basis, management reviews these estimates by comparing them to actual experience and those used by other companies. If a change in an estimate is made, the carrying value of these assets and liabilities may have to be adjusted. Differences in the discount rate and expected long-term rate of return on plan assets within reasonably likely ranges would have had the following estimated impact on 2007 results:

(Thousands of dollars)		Pension Benefits		Other Benefits
Discount rate				
Effect of change on net periodic benefit cost (income):				
.25 percentage point increase	$	(118)	$	(6)
.25 percentage point decrease		121		6
Effect of change on PBO/APBO:				
.25 percentage point increase	$	5,044	$	172
.25 percentage point decrease		(4,810)		(166)
Long-term rate of return on plan assets				
Effect of change on net periodic benefit cost (income):				
.25 percentage point increase	$	(551)	$	-
.25 percentage point decrease		551		-

Forward-Looking Statements and Assumptions

This annual report on Form 10-K contains forward-looking statements and information, within the meaning of the Private Securities Litigation Reform Act of 1995, that are based on management's beliefs as well as assumptions made by and information currently available to management. When used in this report, the words "anticipate," "believe," "estimate," "expect," "plan," "schedule," "could," "may," "might," "should," "project" or similar expressions are intended to identify forward-looking statements. Similarly, statements that describe the Company's future plans, objectives or goals are also forward-looking statements. Such statements reflect the Company's current views with respect to certain events and are subject to certain assumptions, risks and uncertainties, many of which are outside the control of the Company. Undue reliance should not be place on forward-looking statements. These risks and uncertainties include, but are not limited to:

- oil prices;
- declines in domestic and worldwide oil and gas drilling;
- capital spending levels of oil producers;
- the cyclicality of the trailer industry;
- availability and prices for raw materials;
- the inherent dangers and complexities of our operations;
- uninsured judgments or a rise in insurance premiums;
- the inability to effectively integrate acquisitions;
- labor disruptions and increasing labor costs;
- the availability of qualified and skilled labor;
- disruption of our operating facilities or management information systems;
- the impact on foreign operations of war, political disruption, civil disturbance, economic and legal sanctions and changes in global trade policies;
- currency exchange rate fluctuations in the markets in which the Company operates;
- changes in the laws, regulations, policies or other activities of governments, agencies and similar organizations where such actions may affect the production, licensing, distribution or sale of the Company's products, the cost thereof or applicable tax rates;
- costs related to legal and administrative proceedings, including adverse judgments against the Company if the Company fails to prevail in reversing such judgments; and
- general industry, political and economic conditions in the markets where the Company's procures material, components and supplies for the production of the Company's principal products or where the Company's products are produced, distributed or sold.

These and other risks are described in greater detail in "Risk Factors" included elsewhere in this annual report on Form 10-K. All forward-looking statements attributable to the Company or persons acting on its behalf are expressly qualified in their entirety by these factors. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those anticipated, believed, estimated or expected. The Company undertakes no obligations to update or revise its forward-looking statements, whether as a result of new information, future events or otherwise.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

The Company's financial instruments include cash, accounts receivable, accounts payable, invested funds and debt obligations. The book value of accounts receivable, short-term debt and accounts payable are considered to be representative of their fair market value because of the short maturity of these instruments. The Company's accounts receivable are not concentrated in one customer or industry and are not viewed as an unusual credit risk.

The Company does not utilize financial or derivative instruments for trading purposes or to hedge exposures to interest rates, foreign currency rates or commodity prices. Due to the lack of current debt, the Company does not have any significant exposure to interest rate fluctuations. However, if the Company drew on its line of credit under its Bank Facility, the Company would have exposure since the interest rate is variable. In addition, the Company primarily invoices and purchases in the same currency as the functional currency of its operations, which minimizes exposure to currency rate fluctuations.

The Company is exposed to currency fluctuations with intercompany debt denominated in U.S. dollars owed to the Company's U.S. entity by its Canadian subsidiary. As of December 31, 2007, this inter-company debt was comprised of 8.0 million Canadian dollars. As of December 31, 2007, if the U.S. dollar strengthened by 10% over the Canadian dollar, the net income impact would be $0.5 million of expense and if the U.S. dollar weakened by 10% over the Canadian dollar, the net income impact would be $0.5 million of income. Also, certain assets and liabilities, primarily employee and tax related in Argentina, denominated in the local currency of foreign operations whose functional currency is the U.S. dollar are exposed to fluctuations in currency rates. As of December 31, 2007, if the U.S. dollar strengthened by 10% over these currencies, the net income impact would be $0.1 million of expense and if the U.S. dollar weakened by 10% over these currencies, the net income impact would be $0.1 million of income.

Item 8. Financial Statements and Supplementary Data

Management's Report on Internal Control over Financial Reporting

The management of Lufkin Industries, Inc. (the "Company"), is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) and Rule 15d-15(f) promulgated under the Securities Exchange Act of 1934, as amended). The Company's management assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2007. In making this assessment, the Company's management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in "Internal Control- Integrated Framework."

Based on this assessment, management believes that, as of December 31, 2007, the Company's internal control over financial reporting is effective based on those criteria.

The effectiveness of the Company's internal control over financial reporting as of December 31, 2007, has been audited by Deloitte & Touche LLP, an independent registered accounting firm, as stated in their report which appears herein.

Index to Financial Statements

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of Lufkin Industries, Inc.

We have audited the accompanying consolidated balance sheets of Lufkin Industries, Inc. and subsidiaries (the "Company") as of December 31, 2007 and 2006, and the related consolidated statements of earnings, shareholders' equity and comprehensive income, and cash flows for each of the three years in the period ended December 31, 2007. Our audits also included the financial statement schedule listed in the Index at Item 15. We also have audited the Company's internal control over financial reporting as of December 31, 2007 based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for these financial statements and financial statement schedule, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on these financial statements and the financial statement schedule, and an opinion on the Company's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company and subsidiaries as of December 31, 2007 and 2006, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2007, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, present fairly, in all material respects, the information set forth therein. Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2007, based on the criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

As discussed in Note 1 to the consolidated financial statements, the Company adopted Statement of Financial Accounting Standard ("SFAS") 123(R), *Share-Based Payment*, on January 1, 2006. In addition, the Company adopted SFAS 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans* on December 31, 2006 as discussed in Note 1 to the consolidated financial statements. Furthermore, as discussed in Note 6 to the consolidated financial statements, the Company adopted Financial Interpretation No. 48, *Accounting for Uncertainty in Income Taxes- an Interpretation of SFAS No. 109* on January 1, 2007.

DELOITTE & TOUCHE LLP

Houston, Texas
February 29, 2008

LUFKIN INDUSTRIES, INC.
CONSOLIDATED BALANCE SHEETS

December 31, 2007 and 2006
(Thousands of dollars, except share and per share data)

	2007	2006
Assets		
Current Assets:		
Cash and cash equivalents	$ 95,748	$ 57,797
Receivables, net	93,634	90,585
Income tax receivable	4,637	-
Inventories	95,821	85,630
Deferred income tax assets	1,615	7,919
Other current assets	1,412	1,521
Total current assets	292,867	243,452
Property, plant and equipment, net	120,129	113,081
Prepaid pension costs	71,571	56,856
Goodwill, net	11,990	11,732
Other assets, net	4,099	3,948
Total assets	$ 500,656	$ 429,069
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable	$ 23,977	$ 24,375
Accrued liabilities:		
Payroll and benefits	11,444	9,810
Warranty expenses	3,641	3,668
Taxes payable	7,131	7,665
Other	21,941	15,977
Total current liabilities	68,134	61,495
Deferred income tax liabilities	34,600	28,022
Postretirement benefits	7,303	8,475
Other liabilities	5,966	2,937
Commitments and contingencies	-	-
Shareholders' equity:		
Common stock, $1.00 par value per share; 60,000,000 shares authorized; 15,534,184 and 15,322,903 shares issued and outstanding, respectively	15,534	15,323
Capital in excess par	48,315	38,173
Retained earnings	341,315	280,198
Treasury stock, 895,278 and 395,278 shares, respectively, at cost	(31,580)	(4,083)
Accumulated other comprehensive income (loss)	11,069	(1,471)
Total shareholders' equity	384,653	328,140
Total liabilities and shareholders' equity	$ 500,656	$ 429,069

See notes to consolidated financial statements.

LUFKIN INDUSTRIES, INC.
CONSOLIDATED STATEMENTS OF EARNINGS

Years ended December 31, 2007, 2006 and 2005
(Thousands of dollars, except per share data)

	2007	2006	2005
Sales	$ 597,187	$ 605,492	$ 492,167
Cost of sales	430,819	449,243	378,826
Gross profit	166,368	156,249	113,341
Selling, general and administrative expenses	59,034	52,994	44,135
Operating income	107,334	103,255	69,206
Interest income	3,751	1,893	563
Interest expense	(285)	(160)	(159)
Other income (expense), net	1,926	(259)	(335)
Earnings before income tax provision	112,726	104,729	69,275
Income tax provision	38,515	31,735	24,731
Net earnings	74,211	72,994	44,544
Net earnings per share			
Basic	$ 4.98	$ 4.92	$ 3.10
Diluted	$ 4.92	$ 4.83	$ 3.03

See notes to consolidated financial statements.

LUFKIN INDUSTRIES, INC.
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY & COMPREHENSIVE INCOME

Years Ended December 31, 2007, 2006 and 2005 (Thousands of dollars, except share data)	Common Stock Shares, net of Treasury	Common Stock	Capital In Excess of Par	Retained Earnings	Treasury Stock	Compre-hensive Income	Accumulated Other Compre-hensive Income (Loss)	Total
Balance, Jan. 1, 2005	13,980,680	14,472	19,488	177,374	(5,075)		2,673	208,932
Comprehensive income:								
Net earnings				44,544		44,544		44,544
Other comprehensive income, net of tax:								
Foreign currency translation adjustments						(727)		(727)
Other comprehensive income						(727)	(727)	
Comprehensive income						43,817		
Cash dividends				(5,491)				(5,491)
Exercise of stock options	744,686	653	12,217		951			13,821
Balance, Dec. 31, 2005	14,725,366	15,125	31,705	216,427	(4,124)		1,946	261,079
Comprehensive income:								
Net earnings				72,994		72,994		72,994
Other comprehensive income, net of tax:								
Foreign currency translation adjustments						1,012	1,012	1,012
Total comprehensive income						$74,006		
Initial application of FAS 158:								
Defined benefit pension plans							(5,758)	
Defined benefit postretirement plans							1,329	
Total initial application of FAS 158:							(4,429)	(4,429)
Cash dividends				(9,223)				(9,223)
Stock-based compensation			2,908					2,908
Exercise of stock options	202,259	198	3,560		41			3,799
Balance, Dec. 31, 2006	14,927,625	$15,323	$ 38,173	$280,198	$ (4,083)		$ (1,471)	$ 328,140
Comprehensive income:								
Net earnings				74,211		74,211		74,211
Other comprehensive income, net of tax:								
Foreign currency translation adjustments						5,057	5,057	5,057
Defined benefit pension plans						6,979	6,979	6,979
Defined benefit post-retirement plans						504	504	504
Total comprehensive income						$86,751		
Cash dividends				(13,094)				(13,094)
Treasury stock purchases	(500,000)				(27,497)			(27,497)
Stock-based compensation			3,682					3,682
Exercise of stock options	211,281	211	6,460					6,671
Balance, Dec. 31, 2007	14,638,906	$15,534	$ 48,315	$341,315	$(31,580)		$ 11,069	$ 384,653

See notes to consolidated financial statements.

LUFKIN INDUSTRIES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended December 31, 2007, 2006 and 2005
(Thousands of dollars)

	2007	2006	2005
Cash flows form operating activities:			
Net earnings	$ 74,211	$ 72,994	$ 44,544
Adjustments to reconcile net earnings to cash provided by operating activities:			
Depreciation and amortization	14,524	11,950	11,376
Deferred income tax provision/benefit	8,795	(4,520)	(2,041)
Excess tax benefit from share-based compensation	(3,031)	(3,525)	-
Share-based compensation expense	3,682	2,908	-
Pension income	(3,257)	(2,901)	(2,115)
Postretirement benefits/obligation	(400)	(123)	747
(Gain) loss on disposition of property, plant and equipment	(450)	(123)	92
Changes in:			
Receivables, net	(1,141)	(9,440)	(19,905)
Income tax receivable	(4,573)	-	-
Inventories	(7,549)	(10,490)	(20,360)
Other current assets	179	3,553	(3,533)
Accounts payable	(2,425)	3,039	(2,367)
Accrued liabilities	11,745	4,044	17,242
Net cash provided by operating activities	90,310	67,366	23,680
Cash flows from investing activites:			
Additions to property, plant and equipment	(19,253)	(31,241)	(15,803)
Proceeds from disposition of property, plant and equipment	1,395	236	187
Increase in other assets	(231)	(680)	(833)
Acquisition of other companies	-	-	(3)
Net cash used in investing activities	(18,089)	(31,685)	(16,452)
Cash flows from financing activites:			
Payments of short-term notes payable	-	(288)	(1,530)
Dividends paid	(13,094)	(9,223)	(5,491)
Excess tax benefit from share-based compensation	3,031	3,525	-
Proceeds from exercise of stock options	3,467	2,192	8,564
Purchases of treasury stock	(27,497)	-	-
Net cash provided by (used in) financing activities	(34,093)	(3,794)	1,543
Effect of translation on cash and cash equivalents	(177)	88	(46)
Net increase in cash and cash equivalents	37,951	31,975	8,725
Cash and cash equivalents at beginning of period	57,797	25,822	17,097
Cash and cash equivalents at end of period	$ 95,748	$ 57,797	$ 25,822

See notes to consolidated financial statements.

LUFKIN INDUSTRIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) Corporate Organization and Summary of Significant Accounting Policies
Lufkin Industries, Inc. and its consolidated subsidiaries (collectively, the "Company") manufacture and sell oil field pumping units, power transmission products and highway trailers throughout the world.

Principles of consolidation: The consolidated financial statements include the accounts of Lufkin Industries, Inc. and its consolidated subsidiaries after elimination of all inter-company accounts and transactions.

Use of estimates: The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

Foreign currencies: Assets and liabilities of foreign operations where the applicable foreign currency is the functional currency are translated into U.S. dollars at the exchange rate in effect at the end of each accounting period, with any resulting gain or loss reflected in accumulated other comprehensive income in the shareholders' equity section of the balance sheet. Income statement accounts are translated at the average exchange rates prevailing during the period. Gains and losses resulting from balance sheet remeasurement of foreign operations where the U.S. dollar is the functional currency are included in the consolidated statement of earnings as incurred.

Any gains or losses on transactions denominated in a foreign currency are included in the consolidated statements of earnings as incurred.

Cash equivalents: The Company considers all highly liquid investments with maturities of three months or less when purchased to be cash equivalents.

Revenue recognition: Revenue is not recognized until it is realized or realizable and earned. The criteria to meet this guideline are: persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the price to the buyer is fixed or determinable and collectibility is reasonably assured. The Company will process a Bill-and-Hold invoice and recognize revenue at the time of the storage request if all of the following criteria are met:

- The customer has accepted title and risk of loss;
- The customer has provided a written purchase order for the product;
- The customer, not the Company, requested the product to be stored and to be invoiced under a Bill-and-Hold arrangement. The customer must also provide the business purpose for the storage request;
- The customer must provide a storage period and future shipping date;
- The Company must not have retained any future performance obligations on the product;
- The Company must segregate the stored product and not make it available to use on other orders; and
- The product must be completed and ready for shipment.

Amounts billed for shipping are classified as sales and costs incurred for shipping are classified as cost of sales in the consolidated statements of earnings.

Accounts & Notes Receivable and Allowance for Doubtful Accounts: Accounts and notes receivable are stated at the historical carrying amount net of write-offs and allowance for doubtful accounts. The Company establishes an allowance for doubtful accounts based on historical experience and any specific customer issues that the Company has identified. Uncollected receivables are generally reserved before being past due over one year or when the Company has determined that the balance will not be collected.

Inventories: The Company reports its inventories by using the last-in, first-out (LIFO) and the first-in, first-out (FIFO) methods less reserves necessary to report inventories at the lower of cost or estimated market. Inventory costs include material, labor and factory overhead. On a routine basis, the Company uses estimates in determining the level of reserves required to state inventory at the lower of cost or market. Management's estimates are primarily influenced by market activity levels, production requirements, the physical condition of products and technological innovation. Changes in any of these factors may result in adjustments to the carrying value of inventory.

(1) Corporate Organization and Summary of Significant Accounting Policies (Continued)

Property, plant and equipment (P. P. & E.): The Company records investments in these assets at cost. Improvements are capitalized, while repair and maintenance costs are charged to operations as incurred. Gains or losses realized on the sale or retirement of these assets are reflected in income. The Company periodically reviews its P. P. & E. for possible impairment whenever events or changes in circumstance might indicate that the carrying amount of an asset may not be recoverable. An impairment loss is recognized if the carrying amount of a long-lived asset is not recoverable and exceeds its fair value. The carrying amount of a long-lived asset is not recoverable if it exceeds the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the asset. Depreciation for financial reporting purposes is provided on a straight-line method based upon the estimated useful lives of the assets. Accelerated depreciation methods are used for tax purposes. The following is a summary of the Company's P. P. & E. useful lives:

	Useful Life (in years)
Land	-
Land improvements	10.0 - 25.0
Buildings	12.5 - 40.0
Machinery and equipment	3.0 - 15.0
Furniture and fixtures	5.0 - 12.5
Computer equipment and software	3.0 - 7.0

Goodwill and other intangible assets: Goodwill and intangible assets with indefinite lives are not amortized, and are and tested for impairment at least annually. During the first quarter of 2007, the Company completed its annual impairment evaluation by comparing the fair value of each reporting unit to its carrying amount. Since the fair value of each reporting unit exceeded the carrying value, no impairment was recorded.

The Company amortizes intangible assets with finite lives over the years expected to be benefited.

Income taxes: The Company computes taxes on income in accordance with the tax rules and regulations of the many taxing jurisdictions where the income is earned. The income tax rates imposed by these taxing authorities vary substantially. Taxable income may differ from pretax income for financial accounting purposes. To the extent that differences are due to revenue or expense items reported in one period for tax purposes and in another period for financial accounting purposes, an appropriate provision for deferred income taxes is made. Any effect of changes in income tax rates or tax laws are included in the provision for income taxes in the period of enactment. When it is more likely than not that a portion or all of a deferred tax asset will not be realized in the future, the Company provides a corresponding valuation allowance against deferred tax assets.

The Company's tax filings are subject to regular audit by the tax authorities in most of the jurisdictions in which it conducts business. These audits may result in assessments for additional taxes which are resolved with the authorities or, potentially, through the courts. Tax liabilities are recorded based on estimates of additional taxes which will be due upon the conclusion of these audits. Estimates of these tax liabilities are made based upon prior experience and are updated in light of changes in facts and circumstances. However, due to the uncertain and complex application of tax regulation, it is possible that the ultimate resolution of audits may result in liabilities which could be materially different from these estimates. In such an event, the Company will record additional tax expense or tax benefit in the year in which such resolution occurs.

Appropriate U.S. and foreign income taxes have been provided for earnings of foreign subsidiary companies that are expected to be remitted in the near future. The cumulative amount of undistributed earnings of foreign subsidiaries that the Company intends to permanently reinvest and upon which no deferred US income taxes have been provided is $47 million at December 31, 2007, the majority of which has been generated in Argentina and Canada. Upon distribution of these earnings in the form of dividends or otherwise, the Company may be subject to US income taxes (subject to adjustment for foreign tax credits) and foreign withholding taxes. It is not practical, however, to estimate the amount of taxes that may be payable on the eventual remittance of these earnings after consideration of available foreign tax credits.

(1) Corporate Organization and Summary of Significant Accounting Policies (Continued)

The Company adopted FIN 48, *Accounting for Uncertainty in Income Taxes—an interpretation of FASB Statement No. 109*, on January 1, 2007. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in accordance with SFAS No. 109, *Accounting for Income Taxes,* by prescribing a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The application of income tax law is inherently complex. The Company is required to determine if an income tax position meets the criteria of more-likely-than-not to be realized based on the merits of the position under tax laws, in order to recognize an income tax benefit. This requires the Company to make many assumptions and judgments regarding merits of income tax positions and the application of income tax law. Additionally, if a tax position meets the recognition criteria of more-likely-than-not the Company is required to make judgments and assumptions to measure the amount of the tax benefits to recognize based on the probability of the amount of tax benefits that would be realized if the tax position was challenged by the taxing authorities. Interpretations and guidance surrounding income tax laws and regulations change over time. As a consequence, changes in assumptions and judgments can materially affect amounts recognized in the consolidated financial statements.

Financial instruments: The Company's financial instruments include cash, accounts receivable, accounts payable and debt obligations. The book value of accounts receivable, short-term debt and accounts payable are considered to be representative of their fair value because of the short maturity of these instruments. As of December 31, 2007 and 2006, the Company had no reportable derivatives.

Stock-based compensation: Beginning January 1, 2006, employee services received in exchange for stock are expensed in accordance with SFAS 123(R), *Share-Based Payment*. The fair value of the employee services received in exchange for stock is measured based on the grant-date fair value. The fair value is determined using the Black-Scholes option-pricing model for the stock option. Awards granted are expensed pro-ratably over the vesting period of the award. As stock based compensation expense is recognized based on awards ultimately expected to vest, compensation expense is reduced for estimated forfeitures based on historical forfeiture rates. SFAS 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods to reflect actual forfeitures.

Prior to January 1, 2006, the Company had elected to follow the accounting provisions of APB No. 25, "Accounting for Stock Issued to Employees," for stock-based compensation and to furnish the pro-forma disclosures required under SFAS No. 148, "Accounting for Stock-Based Compensation- Transition and Disclosures." The Company accounted for its stock option plans under APB Opinion No. 25 under which no compensation cost was recognized. Had compensation cost for these plans been accounted for consistent with SFAS No. 123, "Accounting for Stock-Based Compensation," the Company's net earnings and earnings per share would have been reduced to the following pro forma amounts:

(Thousands of dollars, except per share data)		2005
Net earnings, as reported	$	44,544
Deduct: Total stock-based employee compensation expense determined under SFAS 123 for all awards, net of tax		(1,213)
Pro forma net earnings	$	43,331
Net earnings per share:		
As reported	$	3.10
Pro forma	$	3.02
Diluted net earnings per share		
As reported	$	3.03
Pro forma	$	2.95

(1) Corporate Organization and Summary of Significant Accounting Policies (Continued)

The fair value of each option grant was estimated on the date of grant using the Black-Scholes option-pricing model with the following assumptions:

	2005
Expected dividend yield	0.75% - 1.75%
Expected stock price volatility	38.62% - 44.14%
Risk free interest rate	4.04% - 4.47%
Expected life of options	5 - 8 years

Product warranties: The Company sells certain of its products to customers with a product warranty that provides repairs at no cost to the customer or the issuance of credit to the customer. The length of the warranty term depends on the product being sold, but ranges from one year to five years. The Company accrues its estimated exposure to warranty claims based upon historical warranty claim costs as a percentage of sales multiplied by prior sales still under warranty at the end of any period. Management reviews these estimates on a regular basis and adjusts the warranty provisions as actual experience differs from historical estimates or other information becomes available.

Recently issued accounting pronouncements: In September 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 157 "Fair Value Measurements" ("SFAS 157"). SFAS 157 defines fair value, establishes a framework for measuring fair value in GAAP and expands disclosures about fair value measurements. Prior to SFAS 157, there were different definitions of fair value and limited and dispersed guidance for applying those definitions. SFAS 157 retains the exchange price notion of fair value and clarifies that the exchange price is the price in an orderly transaction between market participants to sell the asset or transfer the liability in the market in which the reporting entity would transact for the asset or liability. SFAS 157 emphasizes that fair value is a market-based measurement, not an entity-specific measurement and establishes a fair value hierarchy that distinguishes between market participant assumptions developed based on market data obtained from independent sources and the reporting entity's own assumptions. SFAS 157 also clarifies that market participant assumptions should include assumptions about risk and the effect of a restriction on the sale or use of an asset. SFAS 157 expands disclosures about the use of fair value to measure assets and liabilities in interim and annual periods and the inputs used to measure fair value. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The provisions of SFAS 157 should be applied prospectively as of the beginning of the fiscal year in which it is initially applied except for certain types of financial instruments. In February 2008, the Financial Accounting Standards Board issued FASB Staff Position ("FSP") No. FAS 157-1 and No. FAS 157-2, which delays the effective date of SFAS 157 for all nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually), to fiscal years beginning after November 15, 2008, and interim periods within those fiscal years, and removes certain leasing transactions from the scope of SFAS 157. The Company is currently evaluating the impact, if any, the adoption of SFAS 157 will have on the fair value measurement of certain investments in its qualified pension plan, but does not expect any significant impact on its consolidated financial position or results of operations.

In December 2007, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 141 (revised 2007) "Business Combinations" ("SFAS 141R"), replacing Statement of Financial Accounting Standards No. 141 "Business Combinations" ("SFAS 141"). SFAS 141R broadens the scope of SFAS 141 by applying the acquisition method of accounting to all transactions and other events in which one entity obtains control over one or businesses and not just business combinations in which control was obtained by transferring consideration. SFAS 141R also modifies the application of the acquisition method. SFAS 141R requires acquired assets and liabilities to be measured at fair value at the acquisition date versus the cost-allocation process used under SFAS 141. This change will require acquisition-related costs and restructuring costs that are expected but not legally obligated to be recognized separately from the acquisition. SFAS 141R also provides revised guidance on accounting for step acquisitions, assets and liabilities arising from contingencies, measuring goodwill and gains from bargain purchases and contingent consideration at the acquisition date. SFAS 141R applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008.

(1) Corporate Organization and Summary of Significant Accounting Policies (Continued)

In December 2007, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 160 "Noncontrolling Interests in Consolidated Financial Statements" ("SFAS 160"). SFAS 160 amends ARB 51 and clarifies that a noncontrolling interest in a subsidiary is an ownership interest in the consolidated entity that should be reported as equity in the consolidated financial statements. SFAS 160 also modifies the income statement presentation of noncontrolling interests, establishes methods of accounting for changes in ownership interests and requires expanded disclosures of noncontrolling interests. SFAS 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008, and will be applied prospectively as of the beginning of the fiscal year in which SFAS 160 is initially applied. The Company does not expect the adoption of SFAS 160 to have a significant impact on its consolidated financial position or results of operations.

Management believes the impact of other recently issued standards, which are not yet effective, will not have a material impact on the Company's consolidated financial statements upon adoption.

(2) Receivables

The following is a summary of the Company's receivable balances at December 31:

(Thousands of dollars)	2007	2006
Accounts receivable	$ 93,293	$ 90,508
Notes receivable	447	472
Other receivables	406	292
Gross receivables	94,146	91,272
Allowance for doubtful accounts receivable	(125)	(215)
Allowance for doubtful notes receivable	(387)	(472)
Net receivables	$ 93,634	$ 90,585

Bad debt expense related to receivables was negligible in 2007, 2006 and 2005, respectively.

(3) Other Current Accrued Liabilities

The following is a summary of the Company's other current accrued liabilities balances at December 31:

(Thousands of dollars)	2007	2006
Customer prepayments	$ 15,370	$ 9,411
Deferred compensation plans	4,650	4,069
Accrued professional services	802	1,057
Other accrued liabilities	1,119	1,440
Total other current accrued liabilities	$ 21,941	$ 15,977

(4) Property, Plant & Equipment

The following is a summary of the Company's P. P. & E. balances at December 31:

(Thousands of dollars)	2007	2006
Land	$ 3,517	$ 3,482
Land improvements	9,398	8,543
Buildings	76,095	75,082
Machinery and equipment	235,834	219,783
Furniture and fixtures	5,315	5,007
Computer equipment and software	14,327	14,027
Total property, plant and equipment	344,486	325,924
Less accumulated depreciation	(224,357)	(212,843)
Total property, plant and equipment, net	$ 120,129	$ 113,081

Depreciation expense related to property, plant and equipment was $14.4 million, $11.8 million and $11.3 in 2007, 2006 and 2005, respectively.

(5) Earnings per Share

Earnings per share amounts are based on the weighted average number of shares of common stock and common stock equivalents outstanding during the period. The weighted average number of shares used to compute basic and diluted earnings per share for 2007, 2006 and 2005 is illustrated below:

(Thousands of dollars, except share and per share data)	2007	2006	2005
Numerator:			
Numerator for basic and diluted earnings per share-net earnings	$ 74,211	$ 72,994	$ 44,544
Denominator:			
Denominator for basic net earnings per share weighted-average shares	14,901,176	14,844,514	14,369,934
Effect of dilutive securities: employee stock options	189,187	278,155	315,922
Denominator for diluted net earnings per share adjusted weighted-average shares assumed conversions	15,090,363	15,122,669	14,685,856
Basic net earnings per share	$ 4.98	$ 4.92	$ 3.10
Diluted net earnings per share	$ 4.92	$ 4.83	$ 3.03

Options to purchase a total of 202,302, 134,949 and 86,500 shares of the Company's common stock were excluded from the calculation of fully diluted earnings per share for 2007, 2006 and 2005, respectively, because their effect on fully diluted earnings per share for the period were antidilutive.

(6) Income Taxes

Earnings before income taxes for 2007, 2006 and 2005 consisted of the following:

(Thousands of dollars)	2007	2006	2005
Domestic	$ 89,918	$ 86,536	$ 60,103
Foreign	22,808	18,193	9,172
Total earnings before income taxes	$ 112,726	$ 104,729	$ 69,275

The income tax provision for 2007, 2006 and 2005 consisted of the following:

(Thousands of dollars)	2007	2006	2005
Current:			
U.S. federal and state income taxes	$ 24,296	$ 32,465	$ 23,972
Foreign	5,763	3,919	2,777
Total current	30,059	36,384	26,749
Deferred:			
U.S. federal and state income taxes	8,017	(4,387)	(1,647)
Foreign	439	(262)	(371)
Total deffered	8,456	(4,649)	(2,018)
Total	$ 38,515	$ 31,735	$ 24,731

A reconciliation of the income tax provision as computed at the statutory U.S. income tax rate and the income tax provision presented in the consolidated financial statements is as follows:

(Thousands of dollars)	2007	2006	2005
Tax provision computed at statutory rate	$ 39,454	$ 36,655	$ 24,246
Tax effect of:			
Expenses for which no benefit was realized	467	84	237
Change in effective state tax rate	61	(742)	-
Tax credit	(482)	(1,949)	-
State taxes net of federal benefit	1,086	1,591	1,663
Benefit of export incentives	-	(846)	(677)
Benefit of manufacturing deduction	(1,174)	(629)	(439)
Other, net	(897)	(2,429)	(299)
Total provision for taxes	$ 38,515	$ 31,735	$ 24,731

Cash payments for income taxes totaled $26.7 million, $40.5 million and $12.4 million for 2007, 2006 and 2005, respectively.

(6) Income Taxes (continued)

Net deferred income tax assets and liabilities are comprised of the following:

(Thousands of dollars)	2007	2006
Current defered income tax assets:		
Gross assets	$ 3,881	$ 11,036
Gross liabilities	(2,266)	(3,117)
Total current deferred income tax assets, net	1,615	7,919
Noncurrent defered income tax liabilities:		
Gross assets	8,475	4,949
Gross liabilities	(43,075)	(32,971)
Total noncurrent defered income tax liabilities, net	(34,600)	(28,022)
Net deferred income tax liabilities	$ (32,985)	$ (20,103)

The tax effects of significant temporary differences representing deferred income tax assets and liabilities are as follows:

(Thousands of dollars)	2007	2006
Inventories	$ (931)	$ 5,148
Prepaid pension costs	(23,513)	(18,801)
Payroll and benefits	639	825
Accrued warranty expenses	1,117	1,195
Postretirement benefits	4,923	4,368
Prepaid expenses	(348)	(232)
Depreciation	(13,656)	(12,701)
Accrued liabilities	718	728
Other, net	(1,934)	(633)
Net deferred income tax liabilities	$ (32,985)	$ (20,103)

(6) Income Taxes (continued)

Adoption of FIN 48

The Company adopted FASB Interpretation No. 48 ("FIN 48"), "Accounting for Uncertainty in Income Taxes- an Interpretation of FASB Statement No. 109," on January 1, 2007. As of January 1, 2007, the Company had approximately $3,382,000 of total gross unrecognized tax benefits. Of this total, $2,898,000 (net of the federal benefit on state issues) represents the amount of unrecognized tax benefits that, if recognized, would favorably affect the net effective income tax rate in any future period. As of December 31, 2007, the Company had approximately $2.7 million of total gross unrecognized tax benefits. Of this total, $2.5 million (net of the federal benefit on state issues) represents the amount of unrecognized tax benefits that, if recognized, would favorably affect the net effective income tax rate in any future period. A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows:

(Thousands of dollars)	2007
Balance at January 1, 2007	$ 3,382
Gross increases- current year tax positions	293
Gross increases- tax positions from prior periods	21
Gross decreases- tax positions from prior periods	(648)
Settlements	(306)
Balance at December 31, 2007	$ 2,742

The Company has unrecognized tax positions for which it is reasonably possible that the total amounts of unrecognized tax benefits will significantly increase or decrease within the next twelve months. These unrecognized tax benefits relate to deductions for certain accrued liabilities. The Company expects to initiate procedural steps to resolve these uncertain tax positions and estimates the range of possible change to be $150,000 to $250,000.

The Company conducts business globally and, as a result, Lufkin Industries, Inc. and its subsidiaries file income tax returns in the U.S. federal and state jurisdictions, and various foreign jurisdictions. For U.S. federal purposes, tax years prior to 2002 are closed to assessment and the 2002 tax year is open to examination only to the extent of certain refund claims filed. The 2004 through 2006 tax years remain open to examination by U.S. federal and state authorities. The Company is currently under IRS examination for the 2002-2004 tax years for its amendments to those tax years, the originally filed and amended 2005 tax return, and the originally filed 2006 tax return. The Company expects certain amounts of their U.S. federal FIN 48 liabilities to be settled within the next twelve months. However, the amount of such settlement is not determinable with reasonable possibility at this time. The settlement of such amounts could have a material impact on the financial statements. Statutes for years prior to 2004 remain subject to review in certain U.S. state jurisdictions; however, the outcome of any future audit is not expected to have a material effect on the Company's results of operations. The Company also remains subject to income tax examinations in the following material international jurisdictions: Canada (2003-2006), France (2005-2006), and Argentina (2002-2006).

Lufkin's continuing practice is to recognize interest and penalties related to income tax matters in administrative costs. The Company had $146,000 accrued for interest and penalties at December 31, 2006. Interest of $155,000 was accrued during the twelve months ended December 31, 2007.

(7) Inventories

Inventories used in determining cost of sales were as follows:

(Thousands of dollars)	2007	2006
Gross inventories @ FIFO:		
Finished goods	$ 5,790	$ 7,182
Work in progress	21,674	21,121
Raw materials & component parts	88,722	77,598
Maintenance, tooling & supplies	11,638	10,861
Total gross inventories @ FIFO	127,824	116,762
Less reserves:		
LIFO	30,110	28,888
Valuation	1,893	2,244
Total inventories as reported	$ 95,821	$ 85,630

Gross inventories on a FIFO basis shown above that were accounted for on a LIFO basis were $84.8 million and $82.7 million at December 31, 2007 and 2006, respectively. In 2007, certain inventory quantities associated with the Trailer segment were reduced, resulting in liquidations of LIFO inventory quantities carried at lower costs prevailing in prior years. The effect was to increase net income by approximately $0.5 million.

(8) Goodwill & Acquired Intangible Assets

Balances and related amortization expense for goodwill and acquired intangible assets are as follows:

Acquired Intangible Assets

(Thousands of dollars)	Gross Carrying Amount	Accumulated Amortization
Amortized intangible assets		
Non-compete agreements:		
As of December 31, 2006	$ 515	$ (317)
As of December 31, 2007	604	(493)
Aggregate amortization expense:		
For the year ended 12/31/05	$ 99	
For the year ended 12/31/06	106	
For the year ended 12/31/07	112	
Estimated amortization expense:		
For the year ended 12/31/08	$ 111	
For the year ended 12/31/09	-	
For the year ended 12/31/10	-	
For the year ended 12/31/11	-	
For the year ended 12/31/12	-	

The Company also has multi-year non-compete agreements with certain individuals that are paid and expensed on an annual basis and thus are not recorded as pre-paid assets. Expenses related to these non-compete agreements were $44,000, $75,000 and $75,000 for the years 2007, 2006 and 2005, respectively. These agreements expired in 2007 and no expense is expected in 2008.

(8) Goodwill & Acquired Intangible Assets (continued)

Goodwill

The changes in the carrying amount of goodwill for the year ended December 31, 2007, are as follows:

(Thousands of dollars)	Oil Field	Power Transmission	Trailer	Total
Balance as of 12/31/06	$ 9,432	$ 2,300	$ -	$ 11,732
Foreign currency translation	15	243	-	258
Balance as of 12/31/07	$ 9,447	$ 2,543	$ -	$ 11,990

Goodwill impairment tests were performed in the first quarter of 2007 and no impairment losses were recorded.

(9) Debt Obligations

In 2007, the Company renewed its credit facility with a domestic bank (the "Bank Facility") consisting of an unsecured revolving line of credit that provides for up to $40.0 million of aggregate borrowing. The Bank Facility expires on December 31, 2010. Borrowings under the Bank Facility bear interest, at the Company's option, at either the greater of (i) the prime rate, (ii) the base CD rate plus an applicable margin or (iii) the Federal Funds Effective Rate plus an applicable margin or the London Interbank Offered Rate ("LIBOR") plus an applicable margin, depending on certain ratios as defined in the agreement. The Bank Facility includes customary affirmative and negative covenants, including a minimum tangible net worth, a maximum leverage ratio and a minimum current ratio. As of December 31, 2007, no amounts were outstanding of the $40.0 million of the revolving line of credit. All financial covenants are in compliance under the terms of the Bank Facility. Deducting outstanding letters of credit of $7.1 million, $32.9 million of borrowing capacity was available at December 31, 2007.

The Company's had no long-term notes payable at December 31, 2007 and 2006. Cash payments for debt-related interest totaled zero, $3,000 and $37,000 in 2007, 2006 and 2005, respectively.

(10) Stock Option Plans

On January 1, 2006, the Company adopted SFAS 123-Revised 2004 ("SFAS 123R"), "Share-Based Payment," using the modified prospective method. SFAS 123R is a revision of SFAS No. 123 "Accounting for Stock-Based Compensation," and supersedes APB No. 25, "Accounting for Stock Issued to Employees." The cost of employee services received in exchange for stock based on the grant-date fair value is measured and that the cost is recognized over the period during which the employee is required to provide service in exchange for the award. The fair value is estimated using an option-pricing model. Excess tax benefits, as defined in SFAS 123R, are recognized as additional paid-in-capital.

Under the modified prospective method, the Company began recognizing expense on January 1, 2006, on any unvested awards granted prior to the adoption date of January 1, 2006, expected to vest over the remaining vesting period of the awards. New awards granted after the adoption date will be expensed pro-ratably over the vesting period of the award.

The Company currently has three stock compensation plans that are affected by SFAS 123R. The 1990 Stock Option Plan, the 1996 Nonemployee Director Stock Option Plan and the 2000 Incentive Stock Compensation Plan provide for the granting of stock options to officers, employees and non-employee directors at an exercise price equal to the fair market value of the stock at the date of grant. The 2000 Incentive Stock Compensation Plan also provides for other forms of stock-based compensation such as restricted stock but none have been granted to date. Options granted to employees vest over two to four years and are exercisable up to ten years from the grant date. Upon retirement, any unvested options become exercisable immediately. Options granted to directors vest at the grant date and are exercisable up to ten years from the grant date.

(10) Stock Option Plans (continued)

The following table is a summary of the stock-based compensation expense recognized under SFAS 123R for the years ended December 31, 2007 and 2006, and pro-forma compensation expense had expense been recognized under SFAS 123 for the year ended December 31, 2005:

(Thousands of dollars)	2007	2006	2005
Stock-based compensation expense	$ 3,682	$ 2,908	$ 1,886
Tax benefit	(1,362)	(1,105)	(673)
Stock-based compensation expense, net of tax	$ 2,320	$ 1,803	$ 1,213

The fair value of each option grant during the years ended December 31, 2007, 2006 and 2005 was estimated on the date of grant using the Black-Scholes option-pricing model with the following assumptions:

	2007	2006	2005
Expected dividend yield	1.30% - 1.60%	0.69% - 1.30%	0.75% - 1.75%
Expected stock price volatility	41.10% - 46.20%	44.12% - 48.00%	38.62% - 44.14%
Risk free interest rate	3.71% - 4.85%	4.52% - 5.03%	4.04% - 4.47%
Expected life of options	3 - 6 years	1 - 6 years	5 - 8 years
Weighted-average fair value per share at grant date	$23.48	$22.82	$15.16

The expected life of options was determined based on the exercise history of employees and directors since the inception of the plans. The expected volatility is based upon the historical weekly and daily stock price for the prior number of years equivalent to the expected life of the stock option. The expected dividend yield was based on the dividend yield of the Company's common stock at the date of the grant. The risk free interest rate was based upon the yield of U.S. Treasuries which terms were equivalent to the expected life of the stock option.

A summary of stock option activity under the plans during year ended December 31, 2007, is presented below:

Options	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value ($000's)
Outstanding at January 1, 2007	743,761	$29.06		
Granted	135,350	59.80		
Exercised	(211,281)	16.41		
Forfeited or expired	(8,687)	39.92		
Outstanding at December 31, 2007	659,143	$39.28	7.4	$12,867
Exercisable at December 31, 2007	399,941	$30.87	6.5	$11,095

As of December 31, 2007, there was $3.3 million of total unrecognized compensation expense related to non-vested stock options. That cost is expected to be recognized over a weighted-average period of 2.1 years. The intrinsic value of stock options exercised in 2007, 2006 and 2005 was $9.6 million, $10.5 million and $19.6 million, respectively.

(11) Other Comprehensive Income

The following table illustrates the related tax effect allocated to each component of other comprehensive income:

(Thousands of dollars)	Pre-Tax Amount	Tax (Expense)/ Benefit	Net Amount
Year ended December 31, 2005			
Foreign currency translation adjustments	$ (727)	$ -	$ (727)
Other comprehensive income	$ (727)	$ -	$ (727)
Year ended December 31, 2006			
Foreign currency translation adjustments	$ 1,012	$ -	$ 1,012
Initial application of FAS 158:			
Defined benefit pension plans:			
Net prior service cost	(7,294)	2,553	(4,741)
Net loss	(3,129)	1,095	(2,034)
Net transition asset	1,565	(548)	1,017
Total defined benefit pension plans	(8,858)	3,100	(5,758)
Defined benefit postretirement plans:			
Net gain	2,046	(717)	1,329
Total defined benefit postretirement plans	2,046	(717)	1,329
Other comprehensive income	$ (5,800)	$ 2,383	$ (3,417)
Year ended December 31, 2007			
Foreign currency translation adjustments	$ 5,057	$ -	$ 5,057
Defined benefit pension plans:			
Amortization of net prior service cost	566	(207)	359
Amortization of net loss	102	(37)	65
Amortization of net transition asset	(926)	339	(587)
Net gain arising during period	11,265	(4,123)	7,142
Total defined benefit pension plans	11,007	(4,028)	6,979
Defined benefit postretirement plans:			
Amortization of net gain	(227)	83	(144)
Net gain arising during period	1,022	(374)	648
Total defined benefit postretirement plans	795	(291)	504
Other comprehensive income	$ 16,859	$ (4,319)	$ 12,540

(11) Other Comprehensive Income (continued)

The following table illustrates the balances of accumulated other comprehensive income:

(Thousands of dollars)	Foreign Currency Translation	Defined Benefit Pension Plans	Defined Benefit Postretirement Plans	Accumulated Other Comprehensive Income
Balance, Dec. 31, 2005	$ 1,946	$ -	$ -	$ 1,946
Current-period change	1,012	-	-	1,012
Initial application of FAS 158	-	(5,758)	1,329	(4,429)
Balance, Dec. 31, 2006	2,958	(5,758)	1,329	(1,471)
Current-period change	5,057	6,979	504	12,540
Balance, Dec. 31, 2007	$ 8,015	$ 1,221	$ 1,833	$ 11,069

(12) Stock Repurchase Plan

During 2007, the Company repurchased shares pursuant to several plans approved by the Board of Directors, under which the Company was authorized to spend up to an aggregate of $35.0 million for repurchases of its common stock, including (1) an authorization of $3.0 million made in the third quarter of 1999, (2) an authorization of $2.0 million made in the second quarter of 2003 and (3) an authorization of $30.0 million made in the third quarter of 2007. Repurchased shares are added to treasury stock and are available for general corporate purposes including the funding of the Company's stock option plans. During 2007, 500,000 shares were repurchased under the above plans at an aggregate price of $27.5 million, or an average price of $54.99. As of December 31, 2007, 284,678 shares had been repurchased at an aggregate price of $3.0 million, or $10.54 per share under the 1999 plan, 35,817 shares had been repurchased at an aggregate price of $2.0 million, or $55.84 per share under the 2003 plan and 462,131 shares had been repurchased at an aggregate price of $25.4 million, or $54.91 per share under the 2007 plan. During the fourth quarter of 2007, 100,000 shares were repurchased at an aggregate price of $5.5 million, or $54.61 per share under the 2007 plan. As of December 31, 2007, the Company held 895,278 shares of treasury stock at an aggregate cost of approximately $31.6 million. At December 31, 2007, approximately $4.6 million of repurchase authorizations remained under the 2007 plan. While this repurchase authorization has no expiration date, the Company expects to spend this remaining authorization in 2008.

(13) Capital Stock

The Company is authorized to issue 2,000,000 shares of preferred stock, the terms and conditions to be determined by the Board of Directors in creating any particular series. As of December 31, 2007, no shares of preferred stock had been issued.

(14) Retirement Benefits

The Company has a qualified noncontributory pension plan covering substantially all U.S. employees. The benefits provided by these plans are measured by length of service, compensation and other factors, and are currently funded by trusts established under the plans. Funding of retirement costs for these plans complies with the minimum funding requirements specified by the Employee Retirement Income Security Act, as amended. In addition, the Company has two unfunded non-qualified deferred compensation pension plans for certain U.S. employees. The Pension Restoration Plan provides supplemental retirement benefits. The benefit is based on the same benefit formula as the qualified pension plan except that it does not limit the amount of a participant's compensation or maximum benefit. The Company also provides a Supplemental Executive Retirement Plan that credits an individual with 0.5 years of service for each year of service credited under the qualified plan. The benefits calculated under the non-qualified pension plans are offset by the participant's benefit payable under the qualified plan. The liabilities for the non-qualified deferred compensation pensions plans are included in "Other accrued liabilities" in the Consolidated Balance Sheet.

The Company sponsors two defined benefit postretirement plans that cover both salaried and hourly employees. One plan provides medical benefits, and the other plan provides life insurance benefits. Both plans are contributory, with retiree contributions adjusted periodically. The Company accrues the estimated costs of the plans over the employee's service periods. The Company's postretirement health care plan is unfunded. For measurement purposes, the submitted claims medical trend was assumed to be 9.25% in 1997. Thereafter, the Company's obligation is fixed at the amount of the Company's contribution for 1997.

The Company also has qualified defined contribution retirement plans covering substantially all of its U.S. and Canadian employees. For U.S. employees, the Company makes contributions of 75% of employee contributions up to a maximum employee contribution of 6% of employee earnings. Employees may contribute up to an additional 18% (in 1% increments), which is not subject to match by the Company. For Canadian employees, the Company makes contributions of 3%-8% of an employee's salary with no individual employee match required. All obligations of the Company are funded through December 31, 2007. In addition, the Company provides an unfunded non-qualified deferred compensation defined contribution plan for certain U.S. employees. The Company's and individual's contributions are based on the same formula as the qualified contribution plan except that it does not limit the amount of a participant's compensation or maximum benefit. The contribution calculated under the non-qualified defined contribution plan is offset by the Company's and participant's contributions under the qualified plan. The Company's expense for these plans totaled \$3.3 million, \$3.3 million and \$2.5 million in the years ended December 31, 2007, 2006 and 2005, respectively. The liability for the non-qualified deferred defined contribution plan is included in "Other accrued liabilities" in the Consolidated Balance Sheet.

On December 8, 2003, the "Medicare Prescription Drug, Improvement and Modernization Act of 2003" (the "Act") was signed into law. The Act introduces a prescription drug benefit under Medicare as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit that is at least actuarially equivalent to Medicare Part D. Measures of the accumulated postretirement benefit obligation and net periodic postretirement benefit cost do not reflect any amount associated with the subsidy because the Company's plan is not actuarially equivalent to Medicare Part D and is not expected to receive any subsidy.

(14) Retirement Benefits (Continued)

Obligations and Funded Status
At December 31

(Thousands of dollars)	Pension Benefits 2007	Pension Benefits 2006	Other Benefits 2007	Other Benefits 2006
Changes in benefit obligation				
Benefit obligation at beginning of year	$ 170,861	$ 182,375	$ 9,225	$ 13,087
Service cost	5,452	5,178	174	172
Interest cost	9,725	9,104	458	502
Plan participants' contributions	-	-	1,192	1,045
Actuarial loss (gain)	(6,672)	(18,262)	(1,021)	(3,895)
Benefits paid	(7,921)	(7,534)	(2,102)	(1,686)
Benefit obligation at end of year	171,445	170,861	7,926	9,225
Change in plan assets				
Fair value of plan assets at beginning of year	224,626	209,560	-	-
Actual return on plan assets	22,239	22,567	-	-
Employer contributions	31	33	910	641
Plan participants' contributions	-	-	1,192	1,045
Benefits paid	(7,921)	(7,534)	(2,102)	(1,686)
Fair value of plan assets at end of year	238,975	224,626	-	-
Funded (unfunded) status at end of year	$ 67,530	$ 53,765	$ (7,926)	$ (9,225)

Amounts recognized in the balance sheet consist of:

(Thousands of dollars)	Pension Benefits 2007	Pension Benefits 2006	Other Benefits 2007	Other Benefits 2006
Prepaid pension costs	$ 71,571	$ 56,856	$ -	$ -
Other current accrued liabilities	(241)	(154)	(623)	(750)
Postretirement benefits	-	-	(7,303)	(8,475)
Other non-current liabilities	(3,800)	(2,937)	-	-
	$ 67,530	$ 53,765	$ (7,926)	$ (9,225)

(14) Retirement Benefits (Continued)

Amounts recognized in accumulated other comprehensive income consist of:

(Thousands of dollars)	Pension Benefits 2007	Pension Benefits 2006	Other Benefits 2007	Other Benefits 2006
Prior service cost	$ 4,006	$ 4,741	$ -	$ -
Net loss (gain)	(4,847)	2,034	(1,833)	(1,329)
Transition asset	(380)	(1,017)	-	-
	$ (1,221)	$ 5,758	$ (1,833)	$ (1,329)

The accumulated benefit obligation for all defined benefit pension plans was $159.1 million and $158.4 at December 31, 2007, and 2006, respectively.

Components of Net Periodic Benefit Cost and Other Amounts Recognized in Other Comprehensive Income

(Thousands of dollars)	Pension Benefits 2007	Pension Benefits 2006	Other Benefits 2007	Other Benefits 2006
Net Periodic Benefit Cost				
Service cost	$ 5,452	$ 5,178	$ 174	$ 172
Interest cost	9,725	9,104	458	502
Expected return on plan assets	(17,646)	(16,458)	-	-
Amortization of prior service cost	566	566	-	-
Amortization of net (gain) loss	102	61	(227)	(156)
Amortization of transition asset	(926)	(926)	-	-
Net periodic benefit cost (income)	(2,727)	(2,475)	405	518

Other Changes in Plan Assets and Benefit Obligations Recognized in Other Comprehensive Income

None

The estimated net loss, prior service cost and transition asset for the defined benefit pension plans that will be amortized from accumulated other comprehensive income into net periodic benefit cost over the next fiscal year are $83,000, $566,000 and ($638,000), respectively. The estimated net gain for the defined benefit postretirement plans that will be amortized from accumulated other comprehensive income into net periodic benefit cost over the next fiscal year is ($184,000).

Additional Information

Assumptions

Weighted-average assumptions used to determine benefit obligations at December 31

	Pension Benefits 2007	Pension Benefits 2006	Other Benefits 2007	Other Benefits 2006
Discount rate	6.25% - 6.35%	5.75%	6.20%	5.75%
Rate of compensation increase	4.50%	4.50%	N/A	N/A

(14) Retirement Benefits (Continued)

Weighted-average assumptions used to determine net periodic benefit cost for years ended December 31

	Pension Benefits		Other Benefits	
	2007	2006	2007	2006
Discount rate	5.75%	5.50%	5.75%	5.50%
Expected long-term return on plan assets	8.00%	8.00%	N/A	N/A
Rate of compensation increase	4.50%	4.50%	N/A	N/A

For 2007, the Company assumed a long-term asset rate of return of 8.00%. In developing the 8.00% expected long-term rate of return assumption, the Company evaluated input from its third-party pension plan asset manager, including their review of asset class return expectations and long-term inflation assumptions. The Company also considered its historical 10-year and 15-year compounded return (period ended December 31, 2006), which were in-line to higher than the Company's long-term rate of return assumption, and analyzed expected long-term rate of return projections by asset class.

Assumed health care cost trend rates at December 31

Since the Company's costs for the retiree medical was fixed as of January 1, 1997, no health care cost inflation has been assumed and any change in health care trend rates would not have any impact on the plan's service cost, interest cost or benefit obligation.

Plan Assets

The Company's qualified pension plan weighted-average asset allocations at December 31, 2007, and 2006, by asset category are as follows:

	Target Allocation	Plan Assets At December 31,	
	2008	2007	2006
Equity securities	40% - 70%	56%	53%
Debt securities	30% - 60%	21%	26%
Real estate	0% - 15%	9%	9%
Other	0% - 15%	14%	12%
Total		100%	100%

The Company invests in a diversified portfolio consisting of an array of assets classes that attempts to maximize returns while minimizing volatility. These asset classes include U.S. domestic equities, developed market equities, international equities, fixed income, real estate and hedged investments. Fixed income securities include medium-term government notes, corporate bonds and AAA-rated mortgage-backed securities and collateralized mortgage obligations. Real estate primarily includes REIT investments focused on U.S. commercial warehouses. Hedged investments are primarily concentrated in funds focused on long/short investment strategies.

No equity or debt securities of the Company were held by the plan at December 31, 2007, or 2006.

The unqualified pension plans and the postretirement benefit plan of the Company are unfunded and thus had no plan assets as of December 31, 2007, and 2006.

(14) Retirement Benefits (Continued)

Cash Flows

Contributions

The Company expects to make contributions of $250,000 to the pension plans and expects to make contributions of $642,000 to the postretirement plan in 2008.

Estimated Future Benefit Payments

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid during the fiscal years ending:

(Thousands of dollars)	Pension Benefits	Other Benefits
2008	$ 8,916	$ 642
2009	9,526	666
2010	10,112	681
2011	10,793	697
2012	11,524	705
2013 - 2017	67,169	3,628

(15) Commitments and Contingencies

Legal proceedings: A class action complaint was filed in the U.S. District Court for the Eastern District of Texas on March 7, 1997, by an employee and a former employee who alleged race discrimination in employment. Certification hearings were conducted in Beaumont, Texas in February 1998 and in Lufkin, Texas in August 1998. In April 1999, the District Court issued a decision that certified a class for this case, which included all black employees employed by the Company from March 6, 1994, to the present. The case was closed from 2001 to 2003 while the parties unsuccessfully attempted mediation. Trial for this case began in December 2003, but was postponed by the District Court and was completed in October 2004. The only claims made at trial were those of discrimination in initial assignments and promotions.

On January 13, 2005, the District Court entered its decision finding that the Company discriminated against African-American employees in initial assignments and promotions. The District Court also concluded that the discrimination resulted in a shortfall in income for those employees and ordered that the Company pay those employees back pay to remedy such shortfall, together with pre-judgment interest in the amount of 5%. On August 29, 2005, the District Court determined that the backpay award for the class of affected employees would be $3.4 million (including interest to January 1, 2005) and provided a formula for attorney fees that the Company estimates will result in a total not to exceed $2.5 million. In addition to back pay with interest, the District Court (i) enjoined and ordered the Company to cease and desist all racially biased assignment and promotion practices and (ii) ordered the Company to pay court costs and expenses.

The Company has reviewed this decision with its outside counsel and on September 19, 2005, appealed the decision to the U.S. Court of Appeals for the Fifth Circuit. On April 3, 2007, the Company appeared before the appellate court in New Orleans for oral argument in this case. The three justices in this case will now prepare their decision and the Company believes that after a full and fair review of the evidence, the Court of Appeals will determine that the plaintiffs have not established their claims of discrimination by the Company against the plaintiffs and will enter a decision to that effect and will dismiss the case against the Company. At this time, the Company has concluded that an unfavorable ultimate outcome is not probable. If the District Court's decision is reversed and remanded for a new trial, the Company will vigorously defend itself on retrial. While the ultimate outcome and impact of these claims against the Company cannot be predicted with certainty, the Company believes that the resolutions of these proceedings will not have a material adverse effect on its consolidated financial position. However, should the Company be unsuccessful in its appeal, the final determination could have a material impact on the Company's reported earnings, results of operations and cash flows in a future reporting period.

There are various other claims and legal proceedings arising in the ordinary course of business pending against or involving the Company wherein monetary damages are sought. It is management's opinion that the Company's liability, if any, under such claims or proceedings would not materially affect its consolidated financial position, results of operations or cash flow.

(15) Commitments and Contingencies (continued)

Product warranties: The change in the aggregate product warranty liability for the years ended December 31, 2007 and 2006, is as follows:

(Thousands of dollars)	2007	2006
Beginning balance	$ 3,668	$ 3,245
Claims paid	(3,185)	(2,550)
Additional warranties issued	3,108	3,192
Revisions in estimates	21	(251)
Foreign currency translation	29	32
Ending balance	$ 3,641	$ 3,668

Operating leases: Future minimum rental payments for operating leases having initial or remaining noncancelable lease terms in excess of one year are:

(Thousands of dollars)	
2008	$ 1,118
2009	700
2010	561
2011	268
2012	172
All years	$ 3,020

Expenditures for rentals and leases, including short-term rental contracts, were \$4.2 million, \$2.9 million and \$2.3 million for the years ended December 31, 2007, 2006 and 2005, respectively.

Capital expenditures: As of December 31, 2007, the Company had contractual commitments for capital expenditures of \$10.4 million that are expected to be paid in 2008 and \$0.5 million that are expected to be paid in 2009.

(16) Business Segment Information

The Company operates with three business segments--Oil Field, Power Transmission and Trailer. The three operating segments are supported by a common corporate group. The accounting policies of the segments are the same as those described in the summary of major accounting policies. Corporate expenses and certain assets are allocated to the operating segments primarily based upon third party revenues. Sales by geographic region are determined by the shipping destination of a product or the site of service work. Inter-segment sales and transfers are accounted for as if the sales and transfers were to third parties, that is, at current market prices, as available. The following is a summary of key business segment and product group information:

(Thousands of dollars)	2007	2006	2005
Sales by segment:			
Oil Field	$ 397,354	$ 401,200	$ 307,075
Power Transmission	158,452	124,922	106,616
Trailer	41,381	79,370	78,476
Total sales	$ 597,187	$ 605,492	$ 492,167
Sales by geographic region:			
United States	$ 355,994	$ 428,211	$ 355,631
Europe	49,136	32,789	28,552
Canada	33,277	40,143	34,140
Latin America	83,086	60,049	51,346
Other	75,694	44,300	22,498
Total sales	$ 597,187	$ 605,492	$ 492,167
Earnings (loss) before income taxes:			
Oil Field	$ 83,737	$ 85,325	$ 57,659
Power Transmission	27,160	19,022	13,492
Trailer	(1,797)	(1,661)	(2,454)
Corporate	3,626	2,043	578
Total earnings (loss) before income taxes	$ 112,726	$ 104,729	$ 69,275
Assets by segment:			
Oil Field	$ 218,528	$ 213,854	$ 184,330
Power Transmission	141,566	105,013	87,485
Trailer	22,151	27,582	39,433
Corporate	118,411	82,620	48,547
Total assets	$ 500,656	$ 429,069	$ 359,795
Property, plant & equipmet, net, by geographic region			
United States	$ 84,914	$ 81,385	$ 70,017
Europe	10,947	10,740	6,948
Canada	14,055	11,612	7,309
Latin America	9,926	8,985	8,582
Other	287	359	124
Total P, P & E, net	$ 120,129	$ 113,081	$ 92,980
Capital expenditures by segment			
Oil Field	$ 12,830	$ 19,554	$ 11,815
Power Transmission	5,159	10,486	2,668
Trailer	438	358	523
Corporate	826	843	797
Total capital expenditures	$ 19,253	$ 31,241	$ 15,803
Depreciation/amortization by segment:			
Oil Field	$ 8,578	$ 7,166	$ 6,257
Power Transmission	4,704	3,595	3,662
Trailer	516	636	490
Corporate	726	553	968
Total depreciation/amortization	$ 14,524	$ 11,950	$ 11,377

(16) Business Segment Information (Continued)

Additional key segment information is presented below:

Year Ended December 31, 2007

(Thousands of dollars)	Oil Field	Power Transmission	Trailer	Corporate	Total
Gross sales	$ 399,955	$ 161,731	$ 41,511	$ -	$ 603,197
Inter-segment sales	(2,601)	(3,279)	(130)	-	(6,010)
Net sales	$ 397,354	$ 158,452	$ 41,381	$ -	$ 597,187
Operating income (loss)	$ 82,629	$ 27,122	$ (2,417)	$ -	$ 107,334
Other income (expense), net	1,108	38	619	3,627	5,392
Earnings (loss) before income tax provision	$ 83,737	$ 27,160	$ (1,798)	$ 3,627	$ 112,726

Year Ended December 31, 2006

(Thousands of dollars)	Oil Field	Power Transmission	Trailer	Corporate	Total
Gross sales	$ 404,432	$ 133,674	$ 79,413	$ -	$ 617,519
Inter-segment sales	(3,232)	(8,752)	(43)	-	(12,027)
Net sales	$ 401,200	$ 124,922	$ 79,370	$ -	$ 605,492
Operating income (loss)	$ 85,790	$ 19,126	$ (1,661)	$ -	$ 103,255
Other income (expense), net	(465)	(104)	-	2,043	1,474
Earnings (loss) before income tax provision	$ 85,325	$ 19,022	$ (1,661)	$ 2,043	$ 104,729

Year Ended December 31, 2005

(Thousands of dollars)	Oil Field	Power Transmission	Trailer	Corporate	Total
Gross sales	$ 312,803	$ 112,527	$ 78,480	$ -	$ 503,810
Inter-segment sales	(5,728)	(5,911)	(4)	-	(11,643)
Net sales	$ 307,075	$ 106,616	$ 78,476	$ -	$ 492,167
Operating income (loss)	$ 58,037	$ 13,621	$ (2,452)	$ -	$ 69,206
Other income (expense), net	(378)	(129)	(2)	578	69
Earnings (loss) before income tax provision	$ 57,659	$ 13,492	$ (2,454)	$ 578	$ 69,275

(17) Concentrations of Credit Risk

The Company's concentration with respect to trade accounts receivable is limited. The large number of customers and diversified customer base across the three segments significantly reduces the Company's credit risk. The Company also has strict policies regarding the granting of credit to customers and does not offer credit terms to those customers that do not meet certain financial criteria and other guidelines. At December 31, 2007, 2006 and 2005, one customer represented 14.9%, 11.6% and 8.2%, respectively, of the consolidated Company sales.

(18) Quarterly Financial Data (Unaudited)

The following table sets forth unaudited quarterly financial data for 2007 and 2006:

Quarterly Financial Data (Unaudited)

(Millions of dollars, except per share data)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
2007				
Sales	$ 148.1	$ 144.5	$ 146.9	$ 157.7
Gross profit	40.0	40.3	41.0	45.1
Net earnings	17.8	17.5	19.1	19.8
Basic earnings per share	1.19	1.17	1.28	1.35
Diluted earnings per share	1.17	1.15	1.26	1.34
2006				
Sales	$ 133.4	$ 147.7	$ 158.8	$ 165.6
Gross profit	35.4	39.1	38.7	43.0
Net earnings	15.2	17.4	17.4	23.0
Basic earnings per share	1.03	1.18	1.17	1.54
Diluted earnings per share	1.01	1.16	1.15	1.52

(19) Subsequent Events

In January 2008, the Company announced the decision to suspend its participation in the commercial trailer markets and to develop a plan to run-out existing inventories, fulfill contractual obligations and close all trailer facilities. When the run-out is complete and operations are ceased, the Trailer segment will be treated as a discontinued operation.

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

None

Item 9A. Controls and Procedures

Disclosure Controls and Procedures

Based on their evaluation of the Company's disclosure controls and procedures as of December 31, 2007, the Chief Executive Officer of the Company, Douglas V. Smith, and the Chief Financial Officer of the Company, R. D. Leslie, have concluded that the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and Rule 15d-15(e) promulgated under the Securities Exchange Act of 1934) are effective to ensure that information required to be disclosed in reports that the Company files or submits under the Exchange Act are recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and effective to ensure that information required to be disclosed in such reports is accumulated and communicated to the Company's management, including the Company's principal executive officer and principal financial officer, to allow timely decisions regarding disclosure.

There were no changes in the Company's internal control over financial reporting that occurred during the quarter ended December 31, 2007, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Management's Report on Internal Control over Financial Reporting and the Report of the Independent Registered Public Accounting Firm thereon are set forth in Part II, Item 8 of this report and are incorporated herein by reference.

Item 9B. Other Information

None

PART III

Item 10. Directors and Executive Officers of the Registrant

The information required by Item 10 regarding directors is incorporated by reference from the information under the caption "Nominees for Director" and under the caption "Information About Current and Continuing Directors" in the Company's definitive Proxy Statement for the 2008 Annual Meeting of Stockholders (the "Proxy Statement"), which will be filed within 120 days after December 31, 2007. The information required by Item 10 regarding audit committee financial expert disclosure and the identification of the Company's audit committee is incorporated by reference from the information under the caption "Board Committees" in the section "Information About Current and Continuing Directors" in the Proxy Statement. The information required by Item 10 regarding the disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is incorporated by reference from the information under the caption "Section 16(a) Beneficial Ownership Reporting Compliance" in the Proxy Statement. The information required by Item 10 regarding executive officers is incorporated by reference from the information under the caption "Information About Current Executive Officers" in the Proxy Statement.

The Company has adopted a written code of ethics, entitled the "Code of Ethics for Senior Financial Officers of the Company." The Company requires all its senior financial officers, including the Company's principal executive officer, principal financial officer and principal accounting officer, to adhere to the Code of Ethics for Senior Financial Officers of the Company in addressing the legal and ethical issues encountered in conducting their work. The Company has also adopted a written Corporate Code of Conduct applicable to all salaried employees of the Company, including the senior financial officers. The Company has made available to stockholders the Code of Ethics for Senior Financial Officers of the Company and the Corporate Code of Conduct on its website at www.lufkin.com or a copy can be obtained by writing to the Company Secretary, P.O. Box 849, Lufkin, Texas 75902. Any amendment to, or waiver from, the Code of Ethics for Senior Financial Officers of the Company and the Corporate Code of Conduct will be disclosed in a current report on Form 8-K within four business days of such amendment or waiver as required by the Marketplace Rules of the Nasdaq Stock Market, Inc.

Item 11. Executive Compensation

The information required by Item 11 is incorporated by reference from the information under the captions "Executive Compensation", "Compensation Committee Report", "Stock Option Plans", "Compensation Committee Interlocks and Insider Participation", "Board Committees" and "Director Compensation" in the Proxy Statement.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information required by Item 12 related to security ownership of certain beneficial owners and management and related stockholder matters is incorporated by reference from the information under the caption "Security Ownership of Certain Beneficial Owners and Management" in the Proxy Statement. Information concerning securities authorized for issuance under the Company's equity compensation plans is set forth in Item 5 of this report and is incorporated in Item 12 of this report by reference.

Item 13. Certain Relationships and Related Transactions and Director Independence

During 2007, there were no transactions with management and others, no business relationships regarding directors or nominees for directors and no indebtedness of management required to be disclosed pursuant to this Item 13. The information required by Item 13 related to director independence is incorporated by reference from the information under the caption "Information About Current and Continuing Directors" in the Proxy Statement. The information required by Item 13 regarding related-person transactions is incorporated by reference to the information under the caption "Related Person Transactions" in the Proxy Statement.

Item 14. Principal Accountant Fees and Services

The information required by Item 14 is incorporated by reference from the information under the caption "Report of the Audit Committee" and "Independent Public Accountants" in the Proxy Statement.

PART IV

Item 15. Exhibits and Financial Statement Schedules

(a) Documents filed as part of the report

1. Consolidated Financial Statements

   Report of Independent Registered Public Accounting Firm
   Consolidated Balance Sheets
   Consolidated Statements of Earnings
   Consolidated Statements of Shareholders' Equity & Comprehensive Income
   Consolidated Statements of Cash Flows
   Notes to Consolidated Financial Statements

2. Financial Statement Schedules

   Schedule II- Valuation and Qualifying Accounts

   All other financial statement schedules are omitted because of the absence of conditions under which they are required or because all material information required to be reported are included in the consolidated financial statements and notes thereto.

3. Exhibits

3.1 Fourth Restated Articles of Incorporation, as amended, included as Exhibit 4.1 to Lufkin Industries, Inc.'s (the "Company") registration statement on Form S-8 filed February 17, 2004 (File No. 333-112890), which exhibit is incorporated herein by reference.

3.2 Articles of Amendment to Fourth Restated Articles of Incorporation, included as Exhibit 3.1 to the Company's current report on Form 8-K of the registrant filed December 10, 1999, which exhibit is incorporated herein by reference.

3.3 Amended and Restated Bylaws, included as Exhibit 3.1 to the Company's current report on Form 8-K of the registrant filed October 9, 2007 (File No. 0-02612), which exhibit is incorporated herein by reference.

4.1 Form of Common Stock Certificate, included as Exhibit 4.1 to the Company's quarterly report on Form 10-Q of the registrant filed May 9, 2005 (File No. 0-02612), which exhibit is incorporated herein by reference.

*10.1 1990 Stock Option Plan, included as Exhibit 4.3 to the Company's registration statement on Form S-8 dated August 23, 1995 (File No. 33-62021), which plan is incorporated herein by reference.

*10.2 1996 Nonemployee Director Stock Option Plan, included as Exhibit 4.3 to the Company's registration statement on Form S-8 dated June 28, 1996 (File No. 333-07129), which plan is incorporated herein by reference.

*10.3 Amended and Restated Incentive Stock Compensation Plan 2000, included as Exhibit 10.1 to the Company's current report on Form 8-K dated August 2, 2007 (File No. 0-02612), which exhibit is incorporated herein by reference.

10.4 Credit Agreement, dated December 30, 2002, between Lufkin Industries, Inc., JPMorgan Chase Bank and the lenders party thereto, included as Exhibit 10.1 to the Company's quarterly report on Form 10-Q of the registrant filed May 9, 2005 (File No. 0-02612), which exhibit is incorporated herein by reference.

10.5 Agreement and First Amendment to Credit Agreement, dated June 30, 2004, between Lufkin Industries, Inc. and JPMorgan Chase Bank, included as Exhibit 10.2 to the Company's quarterly report on Form 10-Q of the registrant filed May 9, 2005 (File No. 0-02612), which exhibit is incorporated herein by reference.

10.6 Agreement and Second Amendment to Credit Agreement, dated February 1, 2005, between Lufkin Industries, Inc. and JPMorgan Chase Bank, included as Exhibit to the Company's quarterly report on 10.3 Form 10-Q of the registrant filed May 9, 2005 (File No. 0-02612), which exhibit is incorporated herein by reference.

10.7 Agreement and Third Amendment to Credit Agreement between Lufkin Industries, Inc. and JPMorgan Chase Bank, National Association, included as Exhibit 10.3 to the Company's current report on Form 8-K of the registrant filed February 21, 2006 (File No. 0-02612), which exhibit is incorporated herein by reference.

10.8 Agreement and Fourth Amendment to Credit Agreement between Lufkin Industries, Inc. and JPMorgan Chase Bank, National Association, included as Exhibit 10.1 to the Company's current report on Form 8-K of the registrant filed November 30, 2007 (File No. 0-02612), which exhibit is incorporated herein by reference.

*10.9

Form of General Stock Option Agreement for the Company's 1990 Stock Option Plan, included as Exhibit 10.4 to the Company's quarterly report on Form 10-Q of the registrant filed May 9, 2005 (File No. 0-02612), which exhibit is incorporated herein by reference.

*10.10 Form of Stock Option Agreement with Chief Executive Officer for the Company's 1990 Stock Option Plan, included as Exhibit 10.5 to the Company's quarterly report on Form 10-Q of the registrant filed May 9, 2005 (File No. 0-02612), which exhibit is incorporated herein by reference.

*10.11 Form of Stock Option Agreement for the Company's 1996 Nonemployee Director Stock Option Plan, included as Exhibit 10.6 to the Company's quarterly report on Form 10-Q of the registrant filed May 9, 2005 (File No. 0-02612), which exhibit is incorporated herein by reference.

*10.12 Form of General Stock Option Agreement for the Company's 2000 Incentive Stock Compensation Plan, included as Exhibit 10.7 to the Company's quarterly report on Form 10-Q of the registrant filed May 9, 2005 (File No. 0-02612), which exhibit is incorporated herein by reference.

*10.13 Form of Stock Option Agreement with Chief Executive Officer for the 2000 Incentive Stock Compensation Plan, included as Exhibit 10.8 to the Company's quarterly report on Form 10-Q of the registrant filed May 9, 2005 (File No. 0-02612), which exhibit is incorporated herein by reference.

*10.14 Thrift Plan Restoration Plan for Salaried Employees of Lufkin Industries, Inc., as amended, included as exhibit 10.13 to the Company's annual report on Form 10-K of the registrant filed March 1, 2007 (File No. 0-02612), which exhibit is incorporated herein by reference.

*10.15 Retirement Plan Restoration Plan for Salaried Employees of Lufkin Industries, Inc, as amended, included as exhibit 10.14 to the Company's annual report on Form 10-K of the registrant filed March 1, 2007 (File No. 0-02612), which exhibit is incorporated herein by reference.

*10.16 Lufkin Industries, Inc. Supplemental Retirement Plan, as amended, as amended, included as exhibit 10.15 to the Company's annual report on Form 10-K of the registrant filed March 1, 2007 (File No. 0-02612), which exhibit is incorporated herein by reference.

*10.17 Lufkin Industries, Inc. 2008 Variable Compensation Plan, included as Exhibit 10.1 to Form 8-K filed February 19, 2008 (File No. 0-02612), which exhibit is incorporated herein by reference.

*10.18 Severance Agreement, dated November 11, 1999, between Lufkin Industries, Inc. and Larry M. Hoes, included as Exhibit 10.13 to the Company's quarterly report on Form 10-Q of the registrant filed May 9, 2005 (File No. 0-02612), which exhibit is incorporated herein by reference.

*10.19 Severance Agreement, dated November 11, 1999, between Lufkin Industries, Inc. and John F. Glick, included as Exhibit 10.14 to the Company's quarterly report on Form 10-Q of the registrant filed May 9, 2005 (File No. 0-02612), which exhibit is incorporated herein by reference.

*10.20 Severance Agreement, dated November 11, 1999, between Lufkin Industries, Inc. and Scott H. Semlinger, included as Exhibit 10.15 to the Company's quarterly report on Form 10-Q of the registrant filed May 9, 2005 (File No. 0-02612), which exhibit is incorporated herein by reference.

*10.21 Severance Agreement, dated May 3, 2000, between Lufkin Industries, Inc. and Robert D. Leslie, included as Exhibit 10.16 to the Company's quarterly report on Form 10-Q of the registrant filed May 9, 2005 (File No. 0-02612), which exhibit is incorporated herein by reference.

*10.22 Severance Agreement, dated November 11, 1999, between Lufkin Industries, Inc. and Paul G. Perez, included as Exhibit 10.17 to the Company's quarterly report on Form 10-Q of the registrant filed May 9, 2005 (File No. 0-02612), which exhibit is incorporated herein by reference.

*10.23 Amended and Restated Employment Agreement, dated January 1, 1999, between Lufkin Industries, Inc. and Douglas V. Smith, included as exhibit 10.22 to the Company's annual report on Form 10-K of the registrant filed March 1, 2007 (File No. 0-02612), which exhibit is incorporated herein by reference.

*10.24 Severance Agreement, dated January 16, 1993, between Lufkin Industries, Inc. and Douglas V. Smith, included as Exhibit 10.23 to the Company's annual report on Form 10-K of the registrant filed March 16, 2006 (File No. 0-02612), which exhibit is incorporated herein by reference.

*10.25 Employment Agreement, dated as of August 18, 2006, by and between Lufkin Industries, Inc. and Larry M. Hoes (incorporated by reference to Exhibit 10.1 to Lufkin Industries, Inc.'s Form 8-K (File No. 0-02612) filed on August 24, 2006).

*10.26	Employment Agreement, dated as of August 18, 2006, by and between Lufkin Industries, Inc. and John F. Glick (incorporated by reference to Exhibit 10.1 to Lufkin Industries, Inc.'s Form 8-K (File No. 0-02612) filed on August 24, 2006).
*10.27	Employment Agreement, dated as of August 18, 2006, by and between Lufkin Industries, Inc. and Scott H. Semlinger (incorporated by reference to Exhibit 10.1 to Lufkin Industries, Inc.'s Form 8-K (File No. 0-02612) filed on August 24, 2006).
*10.28	Employment Agreement, dated as of August 18, 2006, by and between Lufkin Industries, Inc. and Paul G. Perez (incorporated by reference to Exhibit 10.1 to Lufkin Industries, Inc.'s Form 8-K (File No. 0-02612) filed on August 24, 2006).
*10.29	Employment Agreement, dated as of August 18, 2006, by and between Lufkin Industries, Inc. and Robert D. Leslie (incorporated by reference to Exhibit 10.1 to Lufkin Industries, Inc.'s Form 8-K (File No. 0-02612) filed on August 24, 2006).
21	Subsidiaries of the registrant
23	Consent of Independent Registered Public Accounting Firm
31.1	Rule 13a-14(a)/15d-14(a) Certification of the Chief Executive Officer
31.2	Rule 13a-14(a)/15d-14(a) Certification of the Chief Financial Officer
32.1	Section 1350 Certification of the Chief Executive Officer certification
32.2	Section 1350 Certification of the Chief Financial Officer certification

* Management contract or compensatory plan or arrangement.

SCHEDULE II

Lufkin Industries, Inc.
Valuation & Qualifying Accounts
(in thousands of dollars)

Description	Balance at Beginning of Year	Additions: Charged to Expense	Additions: Charged to Other Accounts	Deductions	Balance at End of Year
Allowance for Doubtful Receivables:					
Year Ended December 31, 2007	$ 687	(107)	-	68	$ 512
Year Ended December 31, 2006	759	(206)	-	(134)	687
Year Ended December 31, 2005	$ 176	510	-	(73)	$ 759
Inventory: Valuation Reserves:					
Year Ended December 31, 2007	$ 2,244	446	-	797	$ 1,893
Year Ended December 31, 2006	1,171	1,466	-	393	2,244
Year Ended December 31, 2005	$ 1,151	207	-	187	$ 1,171
Inventory: LIFO Reserves:					
Year Ended December 31, 2007	$ 28,888	1,222	-	-	$ 30,110
Year Ended December 31, 2006	24,544	4,344	-	-	28,888
Year Ended December 31, 2005	$ 20,985	3,559	-	-	$ 24,544

SIGNATURES

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

LUFKIN INDUSTRIES, INC.

BY /s/ R. D. Leslie
R. D. Leslie
Signing on behalf of the registrant and as
Vice President/Treasurer/Chief Financial Officer
(Principal Financial and Accounting Officer)

Date: February 29, 2008

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

Name	Title	Date
By /s/ D. V. Smith D. V. Smith	Chief Executive Officer (Principal Executive Officer)	February 29, 2008
By /s/ R. D. Leslie R. D. Leslie	Vice President/Treasurer/Chief Financial Officer (Principal Financial and Accounting Officer)	February 29, 2008
By /s/ J. F. Glick J. F. Glick	Director (President)	February 29, 2008
By /s/ J. F. Anderson J.F. Anderson	Director	February 29, 2008
By /s/ S. V. Baer S. V. Baer	Director	February 29, 2008
By /s/ S. W. Henderson, III S. W. Henderson, III	Director	February 29, 2008
By /s/ J. T. Jongebloed J. T. Jongebloed	Director	February 29, 2008
By /s/ J. H. Lollar J. H. Lollar	Director	February 29, 2008
By /s/ B. H. O'Neal B. H. O'Neal	Director	February 29, 2008
By /s/ H. J. Trout, Jr. H. J. Trout, Jr.	Director	February 29, 2008
By /s/ T. E. Wiener T. E. Wiener	Director	February 29, 2008

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