UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

[X] Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended December 27, 1996 or

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

Commission File No. 1-9249

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

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

4050 Olson Memorial Highway
Golden Valley, Minnesota 55422-5332
(Address of principal executive offices) (Zip Code)

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

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

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

As of March 7, 1997, 17,217,589 shares of Common Stock were outstanding.

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

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

The aggregate market value of approximately 11,059,977 shares held by non-affiliates of the registrant was approximately $344 million on March 7, 1997.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Company's definitive Proxy Statement for its Annual Meeting of Shareholders to be held on May 6, 1997, are incorporated by reference into Part III, as specifically set forth in said Part III.

GRACO INC.

INDEX TO ANNUAL REPORT

ON FORM 10-K

NOTE: Certain exhibits listed in the Index to Exhibits beginning on page 27, and filed with the Securities and Exchange Commission, have been omitted. Copies of such exhibits may be obtained upon written request directed to:

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

PART I

Item 1. Business

General Information. Graco Inc. ("Graco" or "the Company") supplies technology and expertise for the management of fluids in both industrial and commercial settings. Based in Minneapolis, Minnesota, Graco serves customers around the world in the manufacturing, processing, construction and maintenance industries. It designs, manufactures and markets systems, products and technology to move, measure, control, dispense and apply a wide variety of fluids and viscous materials. The Company helps customers solve difficult manufacturing problems, increase productivity, improve quality, conserve energy, save expensive material, control environmental emissions and reduce labor costs. Primary uses of the Company's equipment include the application of coatings and finishes to various industrial and commercial products; the mixing, metering, dispensing and application of adhesive, sealant and chemical bonding materials; the application of paint and other materials to architectural structures; the lubrication and maintenance of vehicles and industrial machinery; and the transferring and dispensing of various fluids. Graco is the successor to Gray Company, Inc., which was incorporated in 1926 as a manufacturer of auto lubrication equipment, and became a public company in 1969.

It is Graco's goal to become the highest quality, lowest cost, most responsive supplier in the world for its principal products. In working to achieve these goals to become a world class manufacturer, Graco continues to organize its manufacturing operations around focused factories which contain product-based cells. Substantial investments in new manufacturing technology have reduced cycle time and improved quality.

The Company operates in one industry segment, namely the design, manufacture, marketing, sale and installation of systems and equipment for the handling of fluids. Financial information concerning geographic operations and export sales for the last three fiscal years is set forth in Note B Consolidated Financial Statements.

Recent Developments. The David A. Koch Center, a world-class manufacturing and global distribution facility, was opened in November 1996 in Rogers, Minnesota. The Koch Center provides additional production capacity and enhanced build-to-order capability for projected growth. All distribution operations conducted by the Company at its distribution center in Brooklyn Center, Minnesota were transferred to the new facility, together with the engineering and manufacturing groups for the Contractor Equipment Division ("CED") and final assembly operations for Industrial pumps. During 1996, the Company's product development efforts resulted in the introduction of approximately 130 new products and packages. To enhance product development efficiencies, the CED Advanced Product Development Group headquartered in Denver, Colorado, was consolidated with the CED Engineering Group in Minneapolis, Minnesota and the Denver facility was closed. The application engineering, manufacturing and customer service functions formerly performed in Franklin Park, Illinois were moved to Minneapolis, Minnesota, in order to realize process improvements in manufacturing and distribution and to take advantage of the enhanced technical capabilities available at the recently expanded Russell J. Gray Technical Center and the Franklin Park facility has closed. Graco is currently constructing a laboratory in its Riverside facility to support the consolidation of product development activities in Minneapolis and to provide world-class demonstration, training, test and display capabilities. This laboratory is expected to be completed during the second quarter of 1997.

Products. Graco manufactures a wide array of specialized pumps, applicators, regulators, valves, meters, atomizing devices, replacement parts, and accessories, which are used in industrial and commercial applications in the movement, measurement, control, dispensing and application of many fluids and semi-solids, including paints, adhesives, sealants, and lubricants. In addition, it offers an extensive line of portable equipment which is used in construction and maintenance businesses for the application of paint and other materials. Graco fluid systems incorporate sophisticated paint circulating and fluid application technology.

Commercial and industrial equipment offered by Graco includes specialized pumps, air and airless spray units, manual finishing equipment and fluid handling systems. A variety of pumps provide fluid pressures ranging from 20 to more than 6,000 pounds per square inch and flow rates from under 1 gallon to 140 gallons per minute. In 1995, Graco introduced a new generation of pumps, which produce higher pressures, have improved corrosion resistance and are easier to service than existing products.

The Company sells accessories for use with its equipment, including hoses, couplings, regulators, valves, filters, reels, meters, and gauges, as well as a complete line of spray guns, tips and applicators. These accessories increase the flexibility, efficiency and effectiveness of Graco equipment. Packings, seals, hoses and other parts, which must be replaced periodically in order to maintain efficiency and prevent loss of material, are also sold by the Company.

Sales of replacement parts and accessories have averaged 45.6 percent of the Company's consolidated net sales and approximately 51.3 percent of gross profits during the last three years. The following table summarizes the consolidated net sales and gross profits (net sales less cost of products sold) by the Company's principal product groups for that same period.

Product Group Sales and Gross Profit (In thousands)	1996		1995		1994	
	$	%	$	%	$	%
NET SALES						
Commercial and industrial equipment	$207,327	52.9%	$206,558	53.5%	$204,584	56.8%
Accessories and replacement parts	184,429	47.1	179,756	46.5	155,429	43.2
	$391,756	100.0%	$386,314	100.0%	$360,013	100.0%
GROSS PROFIT						
Commercial and industrial equipment	$ 92,480	47.2%	$ 90,526	47.7%	$ 89,262	51.3%
Accessories and replacement parts	103,501	52.8	99,101	52.3	84,749	48.7
	$195,981	100.0%	$189,627	100.0%	$174,011	100.0%

Marketing and Distribution. Graco's operations are organized to allow its full line of products and systems to be offered in each of its major geographic markets: the Americas, Europe and Asia Pacific. The Industrial Equipment Division, the Automotive Equipment Division, the Contractor Equipment Division, and the Lubrication Equipment Division provide worldwide marketing direction and product design and application assistance to each of these geographic markets.

Graco sells its equipment worldwide principally through independent distributors. In Canada, Japan, Korea, and Europe, Graco equipment is sold to distribution through sales subsidiaries. In the Americas and Europe, the Company maintains a specialized direct sales force, which handles sales of large systems and sales to certain corporate accounts. Manufacturers' representatives are used with some product lines.

In 1996, Graco's net sales in the Americas were $252,615,000 or approximately 65 percent of the Company's consolidated net sales; in Europe (including the Middle East and Africa) net sales were $78,666,000 or approximately 20 percent; and in the Asia Pacific region, net sales were $60,475,000 or approximately 15 percent.

Consolidated backlog at December 27, 1996, was $19 million compared to $20 million at the end of 1995.

Research, Product Development and Technical Services. Graco's research, development and engineering activities focus on new product design, product improvements, applied engineering and strategic technologies. A dedicated support group of application engineers and technicians also provides specialized technical assistance to customers in the design and evaluation of fluid transfer and application systems. It is one of Graco's financial goals to generate 30 percent of each year's sales from products introduced in the prior three years. To achieve this goal, Graco increased its new product design and application engineering staff, and more than doubled the size of the Russell J. Gray Technical Center in 1995 to provide space for engineering, testing and laboratory activities. During 1996, the CED Advanced Product Development Group, formerly located in Denver, Colorado, was merged with the CED Engineering Group in Minneapolis, and the Engineered Application Solutions Group from Franklin Park, Illinois was consolidated with the Industrial Application Engineering Group in Minneapolis to realize efficiencies in the product development and application engineering processes. Total research and development expenditures were $17,909,000, $15,715,000 and $14,591,000 for the 1996, 1995 and 1994 fiscal years, respectively.

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

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

Environmental Protection. During the fiscal year ending December 27, 1996, the amounts incurred to comply with federal, state and local legislation pertaining to environmental standards did not have a material effect upon the capital expenditures or earnings of the Company.

Employees. As of December 27, 1996, the Company employed approximately 1,997 persons on a full-time basis. Of this total, approximately 332 were employees based outside the United States, and 800 were hourly factory workers in the United States.

Item 2. Properties

As of December 31, 1996, the Company's principal operations that occupy more than 10,000 square feet were conducted in the following facilities:

Type of Facility	Location	Square Footage
Owned		
Distribution/Manufacturing/Office	Rogers, Minnesota	324,000
Manufacturing/Office	Minneapolis, Minnesota	237,600
Manufacturing/Office	Minneapolis, Minnesota	207,000
Engineering/Research & Development	Minneapolis, Minnesota	138,200
Engineering/Manufacturing/Office	Plymouth, Michigan	106,000
Engineering/Manufacturing/Office	Franklin Park, Illinois	82,000
Assembly/European Headquarters/Warehouse	Maasmechelen, Belgium	75,800
Corporate Headquarters	Golden Valley, Minnesota	68,000
Manufacturing/Office	Sioux Falls, South Dakota	55,000
Sales Office/Warehouse	Los Angeles, California	21,000
Office/Warehouse	Mississauga, Ontario, Canada	20,000
Leased		
Engineering/Office/Warehouse	Yokohama, Japan (3 facilities)	48,724
Sales Office	Rungis, France	46,600
Assembly/Engineering/Office/Warehouse	Neuss, Germany	41,765
Technical Publications	Minneapolis, Minnesota	18,200
Sales Office	West Midlands, United Kingdom	16,320
Warehouse	Gwangju-Gun, Korea	10,549

The David A. Koch Center, a new manufacturing and global distribution center located in Rogers, Minnesota, was completed and occupied during the last quarter of 1996. The facility has 324,000 square feet of space and includes office, engineering, research and development, manufacturing, customer service and distribution functions. Functions formerly performed in the Distribution Center (123,800 square feet) in Brooklyn Center, Minnesota, and the Communications Center (18,200 square feet) in Minneapolis, Minnesota, were transferred to the Koch Center, and the leases of these facilities were terminated on December 31, 1996 and February 28, 1997, respectively.

A 21,700 square foot building in Atlanta, Georgia was sold during the last quarter of 1996. The sale of the 82,000 square foot building in Franklin Park, Illinois was completed February 18, 1997. The lease on the Colorado facility (11,600 square feet) terminated on November 30, 1996, and the operations were transferred to Minneapolis, Minnesota. The sales office in Rungis, France will be moved to a smaller facility during the first quarter of 1997.

The Company leases space for subsidiary sales or liaison offices around the world, some of which have demonstration areas and/or warehouse space.

Graco's facilities are in satisfactory condition, suitable for their respective uses and are sufficient and adequate to meet current needs, with the recent and planned expansions. Manufacturing capacity met business demand in 1996. Future production requirements are expected to be met through existing production capabilities, efficiency and productivity improvement and the use of available subcontract services.

Item 3. Legal Proceedings

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

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

No issues were submitted to a vote of security holders during the fourth quarter of 1996.

Executive Officers of the Company

The following are all the executive officers of the Company as of March 7, 1997. There are no family relationships between any of the officers named.

David A. Koch, 66, is Chairman of the Board, a position he has held since 1985. Prior to January 1, 1996, he was also the Chief Executive Officer of the Company, a position he had held since 1962. He joined the Company in 1956 and held various sales and marketing positions with the Company prior to assuming the office of President in 1962. He has served as a director of the Company since 1962.

George Aristides, 61, was elected President and Chief Executive Officer effective January 1, 1996. He became President and Chief Operating Officer in June 1993. From March 1993 to June 1993, he was Executive Vice President, Industrial/Automotive Equipment Division, Manufacturing, Distribution and Eurafrican Operations. From 1985 until 1993, he was Vice President, Manufacturing Operations and Controller. He joined the Company in 1973 as Corporate Controller and became Vice President and Controller in 1980. He has served as a director of the Company since 1993.

Clayton R. Carter, 58, was elected Vice President, Worldwide Industrial Equipment Division, effective December 17, 1996. From January 1, 1995, he was Vice President, Worldwide Lubrication Equipment Division. He became Director, Vehicle Services Division, in February 1994. He joined the Company in 1962 and has held various sales management positions.

James A. Graner, 52, was elected Vice President and Controller in February 1994. He became Treasurer in May 1993. Prior to becoming Assistant Treasurer in 1988, he held various managerial positions in the treasury, accounting and information systems departments. He joined Graco in 1974.

Clyde W. Hansen, 64, was elected Vice President, Human Resources and Quality Management Systems, in December 1993. He joined the Company in 1984 as Employee Relations Director, a position he held until his election.

John L. Heller, 60, was elected Vice President, Latin America & Developing Markets, effective January 4, 1996. From July 1993 to December 1995, he was Senior Vice President and General Manager - Contractor Equipment Division. He became Vice President, Far East Operations and Latin America, in 1992. Prior to becoming Vice President, Far East Operations in 1984, he held various management and staff positions in sales and human resources. He joined the Company in 1972.

Roger L. King, 51, was named Vice President & General Manager, European Operations, effective January 4, 1996. From July 1993 to December 1995, he was Senior Vice President and General Manager - International Operations. He became Senior Vice President and Chief Financial Officer in March 1993, and Vice President and Treasurer in 1987. Prior to becoming Vice President, Treasurer and Secretary in 1980, he held the position of Treasurer and Secretary and various treasury management positions with Graco. He joined the Company in 1970.

David M. Lowe, 41, was elected to the position of Vice President, Worldwide Lubrication Equipment Division, in December 1996. From February 1995 to December 1996, he was Treasurer. Prior to joining the Company, he was employed by Ecolab Inc., where he held various positions in the Treasury Department, including Manager-Corporate Finance; Director, Corporate Finance and most recently Director, Corporate Development.

Robert M. Mattison, 49, was elected Vice President, General Counsel and Secretary, in January 1992, a position which he holds today. Prior to joining the Company, he held various legal positions with Honeywell Inc., most recently as Associate General Counsel.

Mark W. Sheahan, 32, was elected Treasurer, effective December 17, 1996. He joined the Company as Treasury Operations Manager in September 1995. Prior to joining the Company, he held various positions in public accounting with KPMG Peat Marwick LLP and Coopers & Lybrand.

Robert A. Wagner, 46, was elected Vice President, Asia Pacific, of Graco Inc. and President, Graco K.K. effective January 1995. He became Vice President and Treasurer, Graco Inc., in February 1994. He joined the Company in December 1991, as Vice President, Corporate Development and Planning. Prior to joining the Company, he was employed by Texas Instruments for nearly five years, where he held various managerial positions, most recently as Vice President and Manager, Corporate Development.

Thomas J. Fay, 46, was appointed to the position of Vice President, Worldwide Automotive Equipment Division, effective January 4, 1996. During 1995, he was Vice President, European Operations. Prior to becoming General Manager of European Operations in March 1994, he held the position of General Manager, Region III, in Europe. Mr. Fay joined the Company in 1984 and held various sales management positions before moving to Europe in 1990.

Dale D. Johnson, 42, was appointed Vice President, Worldwide Contractor Equipment Division, on December 17, 1996. Prior to becoming the Director of Marketing in June 1996, he held various marketing and sales positions in CED. He joined the Company in 1976.

Charles L. Rescorla, 45, is Vice President, Manufacturing & Distribution Operations, a position to which he was appointed on January 1, 1995. Prior to becoming the Director of Manufacturing in March 1994, he was the Director of Engineering, Industrial Division, a position which he assumed in 1988 when he joined the Company.

The Board of Directors elected Messrs. Koch, Aristides, Graner, Hansen, Heller, King, Mattison and Wagner on May 7, 1996, and Messrs. Carter, Lowe and Sheahan on December 17, 1996, all to hold office until the next annual meeting of directors or until their successors are elected and qualify. Messrs. Fay, Johnson and Rescorla were appointed to their positions by management effective January 4, 1996, December 17, 1996 and January 1, 1995, respectively.

PART II

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

Graco Common Stock. Graco common stock is traded on the New York Stock Exchange under the ticker symbol "GGG." As of March 7, 1997, there were 17,217,589 shares outstanding and 1,984 common shareholders of record, with another estimated 3,100 shareholders whose stock is held by nominees or broker dealers.

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

1996	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Net Sales	$ 90,153	$ 97,099	$ 97,680	$106,824
Gross Profit	44,837	49,422	49,976	51,746
Net Earnings	5,585	10,032	10,157	10,395
Per Common Share:				
Net Earnings	0.32	0.57	0.58	0.60
Dividends Declared	0.12	0.12	0.12	0.14
Stock Price (per share)				
High	$ 20.75	$ 21.63	$ 20.38	$ 26.00
Low	17.75	17.88	18.25	18.50
Volume (# of shares)	1,795.1	1,888.2	1,513.1	1,512.8
1995				
Net Sales	$ 95,527	$103,402	$ 94,797	$ 92,588
Gross Profit	46,527	51,415	46,287	45,398
Net Earnings	5,436	8,532	6,569	7,169
Per Common Share:				
Net Earnings	0.31	0.49	0.37	0.41
Dividends Declared	0.11	0.11	0.11	0.12
Stock Price (per share)				
High	$ 16.17	$ 19.50	$ 23.17	$ 25.50
Low	13.17	16.00	17.42	20.00
Volume (# of shares)	686.9	854.1	1,530.6	1,395.0

Item 6. Selected Financial Data

Graco Inc. & Subsidiaries

(In thousands, except per share amounts)	1996	1995	1994	1993	1992
Net Sales	$391,756	$386,314	$360,013	$322,602	$320,334
Earnings Before Change in Accounting Principles	36,169	27,706	15,326	9,493	11,145
Net Earnings	36,169	27,706	15,326	9,493	5,301
Per Common Share:					
Earnings Before Change in Accounting Principles	$ 2.07	$ 1.59	$ .88	$ .55	$ .65
Net Earnings	2.07	1.59	.88	.55	.31
Total Assets	$247,814	$217,833	$228,385	$216,365	$220,418
Long-term Debt (including current portion)	9,920	12,009	32,483	19,480	22,762
Redeemable Preferred Stock	--	--	1,474	1,485	1,487
Cash Dividends Declared per Common Share	$ 0.50	$ 0.45	$ 0.39	$ 2.15	$ 0.33

1 Includes the special one-time dividend of $1.80 per post-split share declared December 17, 1993.

2 Includes Lockwood Technical, Inc. (LTI), a former wholly-owned subsidiary, sold in 1992.

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

MANAGEMENT'S REVIEW AND DISCUSSION

The following is Management's Review and Discussion and is not covered by the Independent Auditors' Report.

Graco's net earnings of $36.2 million in 1996 are 31 percent higher than the $27.7 million earned in 1995 and are significantly higher than the $15.3 million recorded in 1994. The large increases in 1996 and 1995 primarily reflect a reduced effective tax rate, enhanced profit margins, and higher sales. Operating costs include increased product development expenditures.

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

	Revenue & Expense Item As a Percentage of Net Sales			Revenue & Expense Item Percentage Increase (Decrease)	
	1996	1995	1994	1996/95	1995/94
Net Sales	100.0	100.0	100.0	1	7
Cost of Products Sold	50.0	50.9	51.7	--	6
Product Development	4.6	4.1	4.0	14	8
Selling	21.8	22.4	25.8	(2)	(7)
General & Administrative	10.1	10.9	11.2	(5)	4
Operating Profit	13.5	11.7	7.3	17	71
Interest Expense	(0.2)	(0.6)	(0.5)	(64)	21
Other Income (Expense), Net	0.1	0.2	(0.3)	*	*
Earnings Before Income Taxes	13.4	11.3	6.5	21	86
Income Taxes	4.2	4.1	2.2	5	96
Net Earnings	9.2	7.2	4.3	31	81

* Not a Meaningful Figure

NET SALES

In 1996, Graco recorded its fourth consecutive year of record net sales, posting a 1 percent increase over 1995 to $392 million. The 1996 increase was principally due to an increase in North American sales. Geographically, net sales in the Americas of $253 million in 1996 increased by 6 percent when compared to 1995. With slow economies and weak currencies during most of the year, European sales declined 5 percent in 1996 to $79 million (a 3 percent volume decrease and a 2 percent decline due to exchange rates). Sales in Asia Pacific declined 7 percent in 1996 to $60 million. (Volume was flat and the decline was due to exchange rates.)

In 1995, sales increased 7 percent over 1994, due primarily to higher worldwide sales in all divisions except Contractor Equipment.

Periodic price increases have contributed to net sales. The Company's most recent U.S. price increase was effective in January 1996 and represented an average 2.5 percent increase from its January 1995 price lists. The January 1995 price change was an average 2 percent increase from April 1994 prices.

Consolidated backlog at December 27, 1996 was $19 million compared to $20 million at the end of 1995, and $25 million at the end of 1994.

(In thousands)	1996	1995	1994	% Increase (Decrease) 1996/95	1995/94
Division Sales:					
Industrial Equipment	$154,866	$151,016	$136,995	3	10
Automotive Equipment	69,910	75,637	67,457	(8)	12
Contractor Equipment	124,392	118,818	121,478	5	(2)
Lubrication Equipment	42,588	40,843	34,083	4	20
Consolidated	$391,756	$386,314	$360,013	1	7
Geographic Sales:					
Americas	$252,615	$238,874	$241,169	6	(1)
Europe	78,666	82,552	65,888	(5)	25
Asia Pacific	60,475	64,888	52,956	(7)	23
Consolidated	$391,756	$386,314	$360,013	1	7

COST OF PRODUCTS SOLD

The cost of products sold, as a percentage of net sales, declined in 1996 to 50.0 percent from 50.9 percent in 1995. This decrease was the result of a combination of factors, including modest price increases and improved manufacturing efficiencies, partially offset by material and manufacturing cost increases. In 1995, cost of products sold as a percent of net sales declined from 51.7 percent in 1994, due to a combination of factors including modest price increases.

OPERATING EXPENSES

Operating expenses in 1996 declined 1.0 percent from 1995, due to the impact of lower selling and general and administrative expenses. The lower expense level is also the result of lower non-recurring charges in 1996 when compared to 1995. Operating expenses in 1995 declined 2.2 percent from 1994, due primarily to the impact of Graco's worldwide cost restructuring initiatives, and reduced restructuring charges.

Product development expenses in 1996 increased 14.0 percent over 1995 to $17.9 million. In 1995, product development costs were 7.7 percent higher than 1994 expenditures. These increases reflect Graco's commitment to expanding sales through the development of new products.

FOREIGN CURRENCY EFFECTS

The costs of the Company's products are generally denominated in U.S. dollars, with approximately 11 percent sourced in non-U.S. currencies. A greater proportion of its sales, approximately 35 percent, are denominated in currencies other than the U.S. dollar. As a result, a strengthening of the U.S. dollar decreases sales more than costs and expenses, reducing the Company's gross and operating profits. A weakening of the U.S. dollar has the reverse impact on the Company's gross and operating profits. During 1996, the U.S. dollar was generally stronger against other major currencies, and during 1995, the U.S. dollar was generally weaker against other major currencies. Gains and losses attributable to translating the financial statements for all non-U.S. subsidiaries, and the gains and losses on the forward and option contracts used to hedge these exposures, are included in Other income (expense).

The total effect of exchange rate changes on operating profits plus translation gains and losses included in Other income (expense) decreased earnings before income taxes by $2.7 million in 1996 when compared to 1995 and increased earnings before income taxes by $3.5 million in 1995 when compared to 1994.

OTHER INCOME (EXPENSE)

The Company's interest expense fell in 1996, primarily reflecting a decline in the average levels of debt during the year. This decrease in debt levels is due to the reduction in short-term debt as operating cash flows exceeded working capital and capital investment requirements.

Other income of $0.5 million in 1996 and $0.7 million in 1995, and other expenses of $1.0 million for 1994, respectively, include, among other things, the foreign currency translation gains and losses discussed above, a $1.5 million favorable settlement of an escrow dispute in 1996, and a $0.9 million gain from the sale of unutilized real estate in 1995.

INCOME TAXES

The Company's net effective tax rate of 31 percent in 1996 is four percentage points lower than the 1996 U.S. federal tax rate of 35 percent. The decrease from the 36 percent rate in 1995 is due primarily to foreign earnings being taxed at effective rates lower than the U.S. rate from the utilization of prior net operating losses. The effective tax rate of 36 percent in 1995 was higher than the 1994 rate of 35 percent principally due to the reduced relative effect of U.S. business tax credits. Detailed reconciliations of the U.S. federal tax rate to the effective rates for 1996, 1995, and 1994 are discussed in Note D to the Consolidated Financial Statements.

EARNINGS

In 1996, earnings increased by 31 percent to $36.2 million, or $2.07 per share as compared to 1995, when earnings increased by 81 percent to $27.7 million or $1.59 per share as compared to 1994.

ACCOUNTING CHANGES

The Company adopted Statement of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock Based Compensation" in 1996. Refer to Notes A and H to the Consolidated Financial Statements for more detailed information.

OUTLOOK

Graco anticipates higher sales in 1997, driven primarily by continued new product introductions, an improved worldwide distribution network, satisfactory economic conditions in North America and Europe, and robust growth in the Asia Pacific region other than Japan, which remains stagnant.

Graco has undertaken a number of restructuring efforts in recent years that have improved operating margins and net profit. It is anticipated that these efforts will continue to have a favorable impact on margins and profits in 1997. The Company is looking for additional opportunities to improve operating efficiency.

Currency fluctuations, especially the strength of the U.S. dollar relative to other major currencies, may have an impact on operating margins. In 1997, Graco anticipates a higher effective tax rate.

SAFE HARBOR CAUTIONARY STATEMENT

This annual report on Form 10-K contains "forward-looking statements" about the Company's expectations of the future, which are subject to certain risk factors that could cause actual results to differ materially from those expectations. These factors include economic conditions in the United States and other major world economies, currency exchange fluctuations, and additional factors identified in Exhibit 99 to the Company's Report on Form 10-K for fiscal year 1996.

SHAREHOLDER ACTIONS

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

- - a three-for-two stock split paid in 1996;
- - repurchase of 406,000 shares in 1996;
- - a 17 percent increase in the regular dividend in 1996;
- - a 13 percent increase in the regular dividend in 1995;
- - a 14 percent increase in the regular dividend in 1994.

ASSETS

The following table highlights several key measures of asset performance.

(in thousands)	1996	1995
Cash and Cash Equivalents	$ 6,535	$ 1,643
Working Capital	$63,884	$56,899
Current Ratio	1.8	1.8
Average Days Receivables Outstanding	75	73
Inventory Turnover	4.7	4.3

Average inventory balances decreased during 1996 when compared to 1995; however, year-end inventory was flat at $41.5 million. Accounts receivable increased 14.0 percent to $83.5 million. The increase is primarily due to a combination of factors, including higher fourth quarter consolidated sales.

LIABILITIES

At the end of 1996, the Company's long-term debt (including the current portion thereof) was 7.3 percent of total capital (long-term debt plus shareholders' equity) compared to 10.4 percent in 1995. The Company's total debt (notes payable to banks plus long-term debt including the current portion thereof) as a percentage of capital fell to 9.8 percent at the end of 1996, down from 14.1 percent in 1995. The Company had $66.7 million in unused credit lines available at December 27, 1996. The Company believes that available lines plus operating cash flows are adequate to fund its short and long-term initiatives.

SHAREHOLDERS' EQUITY

Shareholders' equity totaled $126.1 million on December 27, 1996, $22.5 million higher than 1995.

CASH FLOWS FROM OPERATING ACTIVITIES

During 1996, the Company's operating cash flow of $48.6 million was slightly lower than 1995 due to changes in working capital requirements. Cash flow from operating activities in 1995 was $51.7 million, $43.1 million higher than the $8.6 million recorded in 1994.

Cash flows from operating activities have been, and are expected to be, the principal source of funds required for future additions to property, plant, and equipment, and working capital, as well as for other corporate purposes.

CASH FLOWS FROM INVESTING ACTIVITIES

Capital expenditures were $30.0 million in 1996, $19.8 million in 1995, and $23.1 million in 1994. These expenditures have enhanced the Company's engineering and manufacturing capabilities, improved product quality, increased capacity, and lowered costs. Substantial expenditures in 1996 included the construction of the David A. Koch Center located in Rogers, Minnesota, and the addition of manufacturing equipment.

The Company expects to spend in excess of $20 million on capital improvements in 1997. Capital expenditures in 1997 will include manufacturing equipment, and cellular manufacturing and information systems initiatives.

CASH FLOWS FROM FINANCING ACTIVITIES

The amount of common stock issued represents the funds received for shares sold through the Company's Dividend Reinvestment Plan, its Employee Stock Purchase Plan, and the distribution of shares pursuant to its Long Term Stock Incentive Plan, more fully described in Note H to the Consolidated Financial Statements.

Graco offers an Automatic Dividend Reinvestment Plan, which gives shareholders a simple and convenient way to reinvest quarterly cash dividends in additional shares of Graco common stock. Brokerage and service charges are paid by the Company.

All Graco employees in the U.S. participate in the Graco Employee Stock Ownership Plan (ESOP). The final distribution of common shares from the ESOP will be made to eligible U.S. employees in 1997. Eligible employees may also purchase Graco common stock through the Company's Employee Stock Purchase Plan.

From time to time, the Company may make open market purchases of its common shares. On February 23, 1996, the Company's Board of Directors authorized management to repurchase up to 800,000 shares for a period ending on February 28, 1998. In 1996, under this repurchase program, the Company repurchased 406,000 shares at an average price per share of $19.99.

Graco is currently paying 14 cents per share as its regular quarterly dividend. Annual cash dividends paid on the Company's common and preferred stock, were $8.3 million in 1996, $7.5 million in 1995, and $37.7 million in 1994 (including a special one-time dividend of $31.2 million paid on March 21, 1994). The Company expects to continue paying regular quarterly dividends to its common shareholders at amounts which will be adjusted periodically to reflect earnings performance and management expectations.

During 1996, debt was reduced by $2.4 million. Debt was reduced by $27.1 million in 1995, reflecting strong cash flows from operations attributable to higher net income and lower working capital requirements.

In 1995, the Company redeemed all of its 5 percent cumulative preferred stock for approximately $1.5 million.

Item 8. Financial Statements and Supplementary Data

RESPONSIBILITY FOR FINANCIAL REPORTING

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

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

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

INDEPENDENT AUDITORS' REPORT

Shareholders and Board of Directors
Graco Inc.
Minneapolis, Minnesota

We have audited the accompanying consolidated balance sheets of Graco Inc. and Subsidiaries (the "Company") as of December 27, 1996 and December 29, 1995, and the related statements of earnings and cash flows for each of the three years in the period ended December 27, 1996. Our audit also included the financial statement schedule listed in the Index at Item 14. These consolidated financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on the consolidated financial statements and financial statement schedule based on our audits.

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

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Graco Inc. and Subsidiaries as of December 27, 1996 and December 29, 1995, and the results of their operations and their cash flows for each of the three years in the period ended December 27, 1996 in conformity with generally accepted accounting principles. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

Deloitte & Touche LLP
Minneapolis, Minnesota
January 20, 1997

(In thousands, except per share amounts)	Years Ended December 27, 1996	December 29, 1995	December 30, 1994
Net Sales	$ 391,756	$ 386,314	$ 360,013
Cost of products sold	195,775	196,687	186,002
Gross Profit	195,981	189,627	174,011
Product development	17,909	15,715	14,591
Selling	85,281	86,634	92,752
General and administrative	39,734	42,044	40,279
Operating Profit	53,057	45,234	26,389
Interest expense	(831)	(2,335)	(1,923)
Other income (expense), net	543	657	(1,040)
Earnings before Income Taxes	52,769	43,556	23,426
Income taxes	16,600	15,850	8,100
Net Earnings	$ 36,169	$ 27,706	$ 15,326
Net Earnings Per Common Share	$ 2.07	$ 1.59	$ .88

See Notes to Consolidated Financial Statements

(In thousands, except share amounts)	December 27, 1996	December 29, 1995
Assets		
Current Assets:		
Cash and cash equivalents	$ 6,535	$ 1,643
Accounts receivable, less allowances of $4,700 in 1996 and $4,800 in 1995	83,474	73,205
Inventories	41,531	41,693
Deferred income taxes, net	11,633	10,608
Other current assets	1,321	1,333
Total current assets	144,494	128,482
Property, Plant and Equipment, at Cost:		
Land	5,227	3,502
Buildings and improvements	63,213	50,534
Manufacturing equipment	82,544	71,437
Office, warehouse and automotive equipment	31,049	28,578
Construction in progress	1,052	2,117
Total property, plant and equipment, at cost	183,085	156,168
Accumulated depreciation	(88,913)	(79,310)
Net property, plant and equipment	94,172	76,858
Other Assets	9,148	12,493
	$247,814	$217,833

	December 27, 1996	December 29, 1995
Liabilities and Shareholders' Equity		
Current Liabilities:		
Notes payable to banks	$ 3,813	$ 5,051
Current portion of long-term debt	1,845	1,935
Trade accounts payable	13,854	13,849
Salaries, wages and commissions	14,808	14,260
Accrued insurance liabilities	10,925	10,792
Income taxes payable	4,647	4,229
Other current liabilities	30,718	21,467
Total current liabilities	80,610	71,583
Long-term Debt, less current portion	8,075	10,074
Retirement Benefits and Deferred Compensation	33,079	32,605
Commitments and Contingencies (Note J)		
Shareholders' Equity		
Common stock, $1 par value; 22,500,000 shares authorized; shares outstanding, 17,047,166 and 17,264,509, in 1996 and 1995, respectively	17,047	17,265
Additional paid-in capital	22,254	20,397
Retained earnings	85,232	64,949
Other, net	1,517	960
Total shareholders' equity	126,050	103,571
	$247,814	$217,833

See Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS — GRACO INC. & Subsidiaries

(In thousands)	Years Ended December 27, 1996	December 29, 1995	December 30, 1994
Cash Flows from Operating Activities:			
Net earnings	$ 36,169	$ 27,706	$ 15,326
Adjustments to reconcile net earnings to net cash provided by operating activities:			
Depreciation and amortization	12,658	11,082	10,447
Deferred income taxes	781	1,938	(4,042)
Change in:			
Accounts receivable	(10,192)	4,499	(10,806)
Inventories	(394)	9,693	(13,967)
Trade accounts payable	459	(6,193)	2,358
Salaries, wages and commissions	1,081	999	1,439
Retirement benefits and deferred compensation	928	2,448	1,670
Other accrued liabilities	6,963	(3,417)	6,858
Other	148	2,955	(696)
	48,601	51,710	8,587
Cash Flows from Investing Activities:			
Property, plant and equipment additions	(30,038)	(19,848)	(23,100)
Proceeds from sale of property, plant and equipment	1,058	3,036	693
Purchases of marketable securities	--	--	(5,464)
Proceeds from sales of marketable securities	--	--	31,809
	(28,980)	(16,812)	3,938
Cash Flows from Financing Activities:			
Borrowing on notes payable and lines of credit	15,890	44,248	10,411
Payments on notes payable and lines of credit	(16,657)	(50,927)	(2,395)
Proceeds from long-term debt	--	--	16,632
Payments on long-term debt	(1,652)	(20,333)	(5,380)
Common stock issued	2,525	2,485	3,102
Retirement of common and preferred stock	(8,115)	(1,547)	(4,564)
Cash dividends paid	(8,344)	(7,490)	(37,732)
	(16,353)	(33,564)	(19,926)
Effect of exchange rate changes on cash	1,624	(2,135)	(1,250)
Net increase (decrease) in cash and cash equivalents	4,892	(801)	(8,651)
Cash and cash equivalents			
Beginning of year	1,643	2,444	11,095
End of year	$ 6,535	$ 1,643	$ 2,444

See Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
GRACO INC. & Subsidiaries
Years Ended December 27, 1996, December 29, 1995, and December 30, 1994

A. Summary of Significant Accounting Policies

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

Basis of Statement Presentation. The Consolidated Financial Statements include the accounts of the parent company and its subsidiaries after elimination of all significant intercompany balances and transactions. As of December 27, 1996, all subsidiaries are 100 percent owned. Subsidiaries outside North America have been included principally on the basis of fiscal years ended November 30 to effect more timely consolidated financial reporting. The U.S. dollar is the functional currency for all foreign subsidiaries.

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

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

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

Currenty Hedges. The Company periodically evaluates its monetary asset and liability positions denominated in foreign currencies. The Company enters into forward contracts, borrowings in various currencies or options, in order to hedge its net monetary positions. Consistent with financial reporting requirements, these hedges and net monetary positions are recorded at current market values and the gains and losses are included in Other income (expense). The Company believes it uses strong financial counterparts in these transactions and that the resulting credit risk under these hedging strategies is not significant. The notional amounts (which may not be indictative of credit or market risk) of such contracts were (in U.S. dollars) $9,322,000 and $10,226,000 at December 27, 1996 and December 29, 1995, respectively.

Property, Plant and Equipment. For financial reporting purposes, plant and equipment are depreciated over their estimated useful lives, primarily by using the straight-line method as follows: Buildings and improvements 10 to 30 years Leasehold improvements 3 to 10 years Manufacturing equipment and tooling 3 to 10 years Office, warehouse and automotive equipment4 to 10 years

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

Earnings Per Common Share. Earnings per common share are computed on earnings reduced by dividend requirements on preferred stock and based upon the weighted average number of common shares and common equivalent shares, consisting of the dilutive effect of stock options outstanding during each year. Earnings per common share assuming full dilution are substantially the same.

Stock Based Compensation. Statement of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock-Based Compensation," was issued in October 1995 and requires companies to measure employee stock compensation plans based on the fair value method of accounting. However, the statement allows the alternative of continued use of Accounting Principles Board Opinion (APB) No. 25, "Accounting for Stock Issued to Employees," with pro forma disclosure of net income and earnings per share determined as if the fair value method had been applied in measuring compensation cost. The Company adopted SFAS No. 123 in 1996 and elected the continued use of APB No. 25.

B. Industry Segment and Foreign Operations

The Company operates in one industry segment, namely, the design, manufacture, marketing, sale and installation of systems and equipment for the management of fluids.

The Company's operations by geographical area for the last three years are shown below.

(In thousands)	1996	1995	1994
Sales to unaffiliated customers:			
Americas	$ 252,615	$ 238,874	$ 241,169
Europe	78,666	82,552	65,888
Asia Pacific	60,475	64,888	52,956
	391,756	386,314	360,013
Intercompany sales between geographic areas:			
Americas	54,615	56,703	51,939
Europe	57	32	14
Asia Pacific	433	1,398	450
Eliminations	(55,105)	(58,133)	(52,403)
Total sales	$ 391,756	$ 386,314	$ 360,013
Operating profit:			
Americas	$ 71,909	$ 70,037	$ 62,650
Europe	9,153	1,916	(5,463)
Asia Pacific	6,312	4,384	1,639
Eliminations	1,203	1,139	(2,205)
	88,577	77,476	56,621
General corporate expenses and corporate initiatives	(34,977)	(31,585)	(31,272)
Interest expense	(831)	(2,335)	(1,923)
Earnings before income taxes	$ 52,769	$ 43,556	$ 23,426
Assets:			
Americas	$ 180,467	$ 152,831	$ 163,201
Europe	40,938	46,618	50,503
Asia Pacific	26,492	26,985	26,605
Corporate	6,536	1,643	2,444
Eliminations	(6,619)	(10,244)	(14,368)
Total assets	$ 247,814	$ 217,833	$ 228,385

1 Included are U.S. export sales to unaffiliated customers of $27,989, $29,549, and $23,408, in 1996, 1995, and 1994, respectively.

2 Transfers between entities are made at prices which allow appropriate markups to the manufacturing and selling unit.

Net earnings (loss) for subsidiaries operating outside the U.S. were $10,468,000, $12,506,000, and ($5,624,000) for 1996, 1995, and 1994, respectively.

Retained earnings for subsidiaries operating outside the U.S. were $8,872,000 and $4,373,000 for 1996 and 1995, respectively.

Net transaction and translation gains or losses, included in Other income (expense), were ($617,000), $528,000, and $366,000 for 1996, 1995, and 1994, respectively.

C. Inventories

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

(In thousands)	1996	1995
Finished products and components	$ 38,707	$ 40,335
Products and components in various stages of completion	24,691	22,597
Raw materials	15,192	13,152
	78,590	76,084
Reduction to LIFO cost	(37,059)	(34,391)
	$ 41,531	$ 41,693

Inventories valued under the LIFO method were $26,303,000 and $23,783,000 for 1996 and 1995, respectively. All other inventory was valued on the FIFO method.

In 1995, certain inventory quantities were reduced, resulting in liquidation of LIFO inventory quantities carried at lower costs from prior years. The effect was to decrease net earnings in 1995 by approximately $100,000.

D. Income Taxes

Earnings before income tax expense consist of:

(In thousands)	1996	1995	1994
Domestic	$ 33,844	$ 27,247	$ 28,168
Foreign	18,925	16,309	(4,742)
Total	$ 52,769	$ 43,556	$ 23,426

Income tax expense consists of:

(In thousands)	1996	1995	1994
Current:			
Domestic:			
Federal	$ 10,518	$ 9,629	$ 9,383
State and local	1,201	1,591	1,030
Foreign	4,638	3,479	2,596
	16,357	14,699	13,009
Deferred:			
Domestic	(227)	227	(3,617)
Foreign	470	924	(1,292)
	243	1,151	(4,909)
Total	$ 16,600	$ 15,850	$ 8,100

Income taxes paid were $14,967,000, $16,019,000, and $12,136,000 in 1996, 1995, and 1994, respectively.

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

	1996	1995	1994
Statutory tax rate	35%	35%	35%
Foreign earnings with (lower) higher tax rates	(4)	(1)	2
State taxes, net of federal effect	2	2	3
U.S. general business tax credits	(1)	(1)	(3)
Other	(1)	1	(2)
Effective tax rate	31%	36%	35%

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

(In thousands)	1996	1995
Inventory valuations	$ 3,307	$ 3,726
Cost reductions and severance accruals	922	1,115
Insurance accruals	3,669	3,505
Vacation accruals	1,417	1,378
Bad debt reserves	1,281	961
Other	1,037	(77)
Current	11,633	10,608
Unremitted earnings of consolidated foreign subsidiaries	(3,800)	(3,529)
Excess of tax over book depreciation	(4,906)	(3,896)
Postretirement benefits	4,891	4,653
Pension and deferred compensation	5,352	5,666
Net operating loss carryforward	1,272	4,404
Other	594	1,207
Valuation allowance	(1,995)	(5,015)
Non-current	1,408	3,490
Net deferred tax assets	$ 13,041	$ 14,098

1 Payable at the time these earnings are distributed to the parent.

Net non-current deferred tax assets above are included in Other Assets. Total deferred tax assets were $22,247,000 and $23,040,000, and total deferred tax liabilities were $9,206,000 and $8,942,000 on December 27, 1996 and December 29, 1995, respectively. A valuation allowance of $1,995,000 and $5,015,000, has been recorded as of December 27, 1996 and December 29, 1995, respectively, primarily related to the uncertainty of obtaining tax benefits for subsidiary operating losses. The effect of these allowances has been considered in "Foreign earnings with (lower) higher tax rates" in the Company's tax rate reconciliation.

E. Debt

(In thousands)	1996	1995
Term debt, 5.05% at December 27, 1996, payable in equal annual installments through 1997	$ 300	$ 600
Industrial development refunding revenue bonds, 4.65% at December 27, 1996, payable through 2002 (property carried at $3,056 pledged as collateral)	4,000	4,500
Obligations related to low-income housing investments	3,205	4,063
Other	2,415	2,846
Total long-term debt	9,920	12,009
Less current portion	1,845	1,935
Long-term portion	$ 8,075	$10,074

Aggregate annual scheduled maturities of long-term debt for the next five years are as follows: 1997-$1,845,000; 1998-$1,796,000; 1999-$3,295,000; 2000-$1,123,000; 2001-$1,310,000. Interest paid on debt during 1996, 1995, and 1994 amounted to $841,000, $2,179,000, and $1,923,000, respectively. The fair value of the Company's long-term debt at December 27, 1996 and December 29, 1995, is not materially different than its recorded value.

The Company has an interest rate swap agreement in place whereby it fixed the interest rate of the remaining principal amounts of the Company's previously variable interest rate revenue bond debt at 4.65 percent through 1997, at which time the debt will revert back to a variable interest rate. The cash flows related to the swap agreement are recorded as income when received and expense when paid. Market and credit risk are not significant.

On December 27, 1996, the Company had lines of credit with U.S. and foreign banks of $70,379,000, including a $25,000,000 revolving credit agreement. The unused portion of these credit lines was $66,666,000 at December 27, 1996. Borrowing rates under these facilities vary with the prime rate, rates on domestic certificates of deposit, and the London interbank market. The weighted short-term borrowing rates were 3.6 percent and 2.2 percent, at December 27, 1996 and December 29, 1995, respectively. The Company pays commitment fees of up to 3/16 percent per annum on the daily average unused amounts on certain of these lines. No compensating balances are required.

The Company is in compliance with the covenants of its debt agreements. Under the most restrictive terms of the agreements, approximately $19,710,000 of retained earnings were available for payment of cash dividends at December 27, 1996.

F. Shareholders' Equity

Changes in shareholders' equity accounts are as follows:

(In thousands)	1996	1995	1994
Preferred Stock			
Balance, beginning of year	$ --	$ 1,474	$ 1,485
Shares repurchased	--	(1,474)	(11)
Balance, end of year	--	--	1,474
Common Stock			
Balance, beginning of year	17,265	11,377	11,449
Stock split	--	5,754	--
Shares issued	188	143	188
Shares repurchased	(406)	(9)	(260)
Balance, end of year	17,047	17,265	11,377
Additional Paid-In Capital			
Balance, beginning of year	20,397	18,289	19,813
Shares issued	2,337	2,342	2,914
Shares repurchased	(480)	(234)	(4,438)
Balance, end of year	22,254	20,397	18,289
Retained Earnings			
Balance, beginning of year	64,949	50,702	42,430
Net income	36,169	27,706	15,326
Cash dividends declared	(8,657)	(7,705)	(7,054)
Stock split	--	(5,754)	--
Shares repurchased	(7,229)	--	--
Balance, end of year	85,232	64,949	50,702
Other, Net			
Balance, end of year	1,517	960	9
Total Shareholders' Equity	$ 126,050	$ 103,571	$ 81,851

At December 27, 1996, the Company had 22,549 authorized, but not issued, cumulative preferred shares. The Company also has authorized, but not issued, a separate class of 3,000,000 shares of preferred stock, $1 par value.

During 1995, the Company redeemed all 14,740 outstanding shares of cumulative preferred stock at the call price of $105 per share plus accrued and unpaid dividends. Prior to the redemption, the holders of the cumulative preferred stock were entitled to fixed cumulative dividends of 5 percent per annum on the par value before cash dividends were paid or declared on common stock.

The Board of Directors approved a three-for-two stock split on December 15, 1995, effected in the form of a 50 percent stock dividend payable February 7, 1996, to shareholders of record on January 3, 1996. Accordingly, December 29, 1995 balances reflect the split with an increase in common stock and reduction in retained earnings of $5,754,000. All stock option, share, and per share data has been restated to reflect the split.

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

G. Employee Stock Ownership Plan

The Company has a leveraged Employee Stock Ownership Plan (ESOP) under which outstanding debt was $300,000 and $600,000, at December 27, 1996 and December 29, 1995, respectively. This is also the remaining balance of a concurrent loan to the ESOP Trust from the Company on the same terms. The Company's loan is included in long-term debt with the receivable from the ESOP in a like amount recorded as a reduction of shareholders' equity reflected in the Other, net category. The Company is obligated to make annual contributions to the ESOP Trust through 1997 sufficient to repay the loan and interest thereon.

H. Stock Option and Purchase Plans

Stock Option Plans. The Company has a Long Term Stock Incentive Plan, under which a total of 3,475,000 common shares have been reserved for issuance, with 2,129,047 shares remaining reserved at December 27, 1996. Grants under this Plan are in the form of restrictive share awards and stock options. Restrictive share awards of 597,609 common shares have been made to certain key employees under the Plan, such restrictions lapsing in 1997. Compensation cost charged to operations for the restricted share awards was $256,000, $319,000, and $361,000 in 1996, 1995, and 1994, respectively. Stock options for 1,419,603 common shares have also been granted under the Plan. The option price is the market price at the date of grant. Options become exercisable at such time and in such installments as set by the Company, and expire ten years from the date of grant.

In 1996, the shareholders approved a Nonemployee Director Stock Option Plan, under which the Company makes initial and annual grants to the nonemployee directors of the Company. There are 200,000 common shares authorized for issuance under the Plan, 182,000 of which remained reserved at the end of 1996. Nonemployee directors receive an initial option grant of 2,000 shares upon first appointment or election and an annual option grant of 1,500 shares. The exercise price of each option is the fair market value at the date of grant. The options have a ten-year duration and may be exercised in equal installments over four years, beginning one year from the date of grant.

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

	Shares	Weighted Average Exercise Price
Outstanding, December 31, 1993	399,209	$10.43
Granted	387,555	13.06
Exercised	(78,315)	9.37
Canceled	(23,906)	10.17
Outstanding, December 30, 1994	684,543	12.00
Granted	147,144	18.90
Exercised	(38,985)	8.94
Canceled	(88,839)	11.49
Outstanding, December 29, 1995	703,863	13.70
Granted	70,026	19.65
Exercised	(29,120)	12.03
Canceled	(36,241)	12.14
Outstanding, December 27, 1996	708,528	$14.34

The number of stock options exercisable was 232,729, 139,242, and 110,774 at December 27, 1996, December 29, 1995, and December 30, 1994, respectively. These stock options had a weighted average exercise price per share of $11.96, $11.43, and $10.24 at December 27, 1996, December 29, 1995, and December 30, 1994, respectively.

Stock Purchase Plans. Under the Company's Employee Stock Purchase Plan, 3,900,000 common shares have been authorized for sale to employees, 1,064,568 of which remained unissued at the end of 1996. The purchase price of the shares under the Plan is the lesser of 85 percent of the fair market value on the first day or the last day of the Plan year.

In 1994, the shareholders approved a Nonemployee Director Stock Plan which enables individual nonemployee directors of the Company to elect to receive all or part of a director's annual retainer in the form of shares of the Company's common stock instead of cash. The company issued 1,521 and 485 shares under this plan during 1996 and 1995, respectively. No shares were issued during 1994. The expense related to this plan is not significant.

The Company applies Accounting Principles Board Opinion No. 25 and related interpretations in accounting for its stock option and purchase plans. Accordingly, no compensation cost has been recognized for the Employee Stock Purchase Plan and stock options granted under the Long Term Incentive Plan and the Nonemployee Director Stock Option Plan. Compensation cost for these plans determined on the basis of fair value pursuant to SFAS No. 123 is not significant.

I. Retirement Benefits

The Company has a defined contribution plan, under Section 401(k) of the Internal Revenue Code, which provides additional retirement benefits to all U.S. employees who elect to participate. Currently, the Company matches employee contributions at a 50 percent rate, up to 3 percent of the employee's compensation. Employer contributions were $841,000, $852,000 and $850,000 in 1996, 1995, and 1994, respectively.

The Company has noncontributory defined benefit pension plans covering substantially all U.S. employees and directors and most of the employees of the Company's non-U.S. subsidiairies. For the U.S. plans, the benefits are based on years of service and the highest five consecutive years' earnings in the ten years preceding retirement. The Company funds these plans annually in amounts consistent with minimum funding requirements and maximum tax deduction limits and invests primarily in common stocks and bonds, including the Company's common stock. The market value of the plans' investment in the common stock of the Company was $11,070,000 and $9,188,000 at December 27, 1996 and December 29, 1995, respectively. The expenses for these plans consist of the following components:

(In thousands)	1996	1995	1994
Service cost - benefits earned during the period	$ 2,366	$ 2,385	$ 2,499
Interest cost on projected benefit obligation	4,699	4,561	4,301
Actual return on assets	(12,228)	(12,774)	579
Net amortization and deferral	6,254	7,879	(5,583)
Cost of pension plans which are not significant and have not adopted SFAS No. 87	171	65	312
Net periodic pension cost	$ 1,262	$ 2,116	$ 2,108

The plans' funded status and the amounts recognized in the Company's financial statements are summarized below:

(In thousands)	1996 Plans Whose Assets Exceed Accumulated Benefits	1996 Plans Whose Accumulated Benefits Exceed Assets	1995 Plans Whose Assets Exceed Accumulated Benefits	1995 Plans Whose Accumulated Benefits Exceed Assets
Actuarial present value:				
Vested benefit obligation	$ 55,688	$ 4,340	$ 51,266	$ 5,444
Accumulated benefit obligation	$ 60,609	$ 4,772	$ 56,461	$ 5,947
Projected benefit obligation	$ 67,921	$ 6,258	$ 64,240	$ 7,437
Plan assets at fair value	76,797	--	66,182	--
Projected benefit obligation (in excess of) less than plan assets	8,876	(6,258)	1,942	(7,437)
Unrecognized net (gain) loss	(18,553)	43	(11,263)	656
Unrecognized net (asset) liability being amortized	(128)	144	(142)	255
Adjustment required to recognize minimum liability	--	(327)	--	(473)
Accrued pension cost	($ 9,805)	($ 6,398)	($ 9,463)	($ 6,999)

Major assumptions at year-end:

	1996	1995	1994
Discount rate	4 - 7%	4 - 7%	4 - 7 1/2%
Rate of increase in future compensation levels	2 1/2 - 7%	2 1/2 - 7%	3 - 7%
Expected long-term rate of return on plan assets	9%	9%	9%

In addition to providing pension benefits, the Company pays part of the health insurance costs for its retired U.S. employees and their dependents.

The Company's retiree health benefit expense for 1996, 1995, and 1994 was as follows:

(In thousands)	1996	1995	1994
Service cost	$ 457	$ 496	$ 503
Interest cost	924	890	947
Net benefit expense	$ 1,381	$ 1,386	$ 1,450

The Company's policy is to fund these benefits on a pay-as-you-go basis. The actuarial present value of these health benefit obligations and the amount recognized in the consolidated balance sheets were as follows:

(In thousands)	1996	1995
Accumulated postretirement benefit obligation:		
Retirees and beneficiaries	($ 6,000)	($ 4,684)
Fully eligible active plan participants	(2,531)	(2,657)
Other active plan participants	(5,738)	(6,067)
Accumulated benefit obligations	(14,269)	(13,408)
Unrecognized net loss	415	114
Accrued postretirement benefit cost	($ 13,854)	($ 13,294)

The Company's retirement medical benefit plan limits the annual cost increase that will be paid by the Company. In measuring the Accumulated Postretirement Benefit Obligation (APBO), a 6 percent maximum annual trend rate for healthcare costs was assumed for the year ending December 27, 1996. This rate is assumed to remain constant through the year 2001, decline by 1/2 percent for each of the following three years to 4.5 percent and remain at that level thereafter. The discount rate assumption at year-end for 1996, 1995, and 1994 was 7.0 percent, 7.0 percent, and 7.5 percent, respectively. If the assumed healthcare cost trend rate changed by 1 percent, the APBO as of December 27, 1996 would change by 14.4 percent. The effect of a 1 percent change in the cost trend rate on the service and interest cost components of the net periodic postretirement benefits expense would be a change of 16.5 percent.

J. Commitments and Contingencies

Lease Commitments. Aggregate annual rental commitments at December 27, 1996, under operating leases with noncancelable terms of more than one year, were $7,031,000, payable as follows:

(In thousands)	Buildings	Vehicles & Equipment	Total
1997	$ 1,993	$ 751	$ 2,744
1998	1,630	434	2,064
1999	844	187	1,031
2000	492	66	558
2001	182	15	197
Thereafter	437	--	437
	$ 5,578	$ 1,453	$ 7,031

Total rental expense was $3,815,000 for 1996, $4,722,000 for 1995, and $4,103,000 for 1994.

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

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

None.

PART III

Part III, Items 10, 11, 12 and 13, except for certain information relating to Executive Officers included in Part I, is omitted as the Company intends to file with the Securities and Exchange Commission within 120 days of the close of the fiscal year ended December 27, 1996, a definitive proxy statement containing such information pursuant to Regulation 14A of the Securities Exchange Act of 1934 and such information shall be deemed to be incorporated herein by reference from the date of filing such document.

The Company knows of no contractual arrangements which may, at a subsequent date, result in a change in control of the Company.

PART IV

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

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

(1) Financial Statements See Part II

(2) Financial Statement Schedule Page
- Schedule II - Valuation and Qualifying Accounts..................28

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

(3) Management Contract, Compensatory Plan or Arrangement.
(See Exhibit Index.)..30
Those entries marked by an asterisk are Management Contracts, Compensatory Plans or Arrangements

(b) Reports on Form 8-K
There were no reports on Form 8-K for the thirteen weeks ended December 27, 1996.

(c) Exhibit Index...30

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

(In thousands)

Description	Balance at beginning of year	Additions charged to costs and expenses	Deductions from reserves	Balance at end of year
Year ended December 27, 1996:				
Allowance for doubtful accounts	$ 2,800	$ 900	$ 1,300	$ 2,400
Allowance for obsolete and overstock inventory	5,900	2,500	3,300	5,100
Allowance for returns and credits	2,000	4,100	3,800	2,300
Valuation allowance for tax benefits	5,020	--	3,025	1,995
	$15,720	$ 7,500	$ 11,425	$11,795
Year ended December 29, 1995:				
Allowance for doubtful accounts	$ 2,700	$ 700	$ 600	$ 2,800
Allowance for obsolete and overstock inventory	6,400	1,400	1,900	5,900
Allowance for returns and credits	2,000	3,400	3,400	2,000
Valuation allowance for tax benefits	6,900	--	1,880	5,020
	$18,000	$ 5,500	$ 7,780	$15,720
Year ended December 30, 1994:				
Allowance for doubtful accounts	$ 2,200	$ 1,200	$ 700	$ 2,700
Allowance for obsolete and overstock inventory	5,500	3,100	2,200	6,400
Allowance for returns and credits	1,900	2,000	1,900	2,000
Valuation allowance for tax benefits	2,740	4,160	--	6,900
	$12,340	$10,460	$ 4,800	$18,000

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

2 Items scrapped or otherwise disposed of during the year.

3 Credits issued and returns processed, related to prior years.

Signatures

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

Graco Inc.

/s/GEORGE ARISTIDES	March 19, 1997
George Aristides President and Chief Executive Officer	

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

/s/GEORGE ARISTIDES	March 19, 1997
George Aristides President and Chief Executive Officer (Principal Executive Officer)	
/s/MARK W. SHEAHAN	March 19, 1997
Mark W. Sheahan Treasurer (Principal Financial Officer)	
/s/JAMES A. GRANER	March 19, 1997
James A. Graner Vice President and Controller (Principal Accounting Officer)	

D. A. Koch	Director, Chairman of the Board
G. Aristides	Director, President and Chief Executive Officer
R. O. Baukol	Director
R. D. McFarland	Director
L. R. Mitau	Director
M. A.M. Morfitt	Director
D. R. Olseth	Director
C. M. Osborne	Director
W. G. Van Dyke	Director

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

/s/GEORGE ARISTIDES	March 19, 1997
George Aristides (For himself and as attorney-in-fact)	

Exhibit Index

Exhibit Number	Description
3.1	Restated Articles of Incorporation. See also Exhibit 4.3.
3.2	Restated Bylaws. (Incorporated by reference to Exhibit 2 to the Company's Report on Form 8-K dated January 12, 1988.)
3.3	Bylaws Amendment. (Incorporated by reference to Exhibit 1 to the Company's Report on Form 8-K dated March 1, 1990.)
4.1	Credit Agreement dated October 1, 1990, between the Company and First Bank National Association. (Incorporated by reference to Exhibit 5 to the Company's Report on Form 10-Q for the thirty-nine weeks ended September 28, 1990.)
4.2	Amendment 1 dated June 12, 1992, to Credit Agreement dated October 1, 1990, between the Company and First Bank National Association; and Amendment 2 dated December 31, 1992, to the same Agreement. (Incorporated by reference to Exhibit 1 to the Company's Report on Form 8-K dated March 11, 1993.) Amendment 3 dated November 8, 1993, and Amendment 4, dated February 8, 1994. (Incorporated by reference to Exhibit 4.2 to the Company's 1993 Annual Report on Form 10-K.) Amendment 5, dated April 10, 1995. (Incorporated by reference to Exhibit 4.2 to the Company's 1995 Annual Report on Form 10-K.) Amendment 6, dated September 27, 1996. (Incorporated by reference to Exhibit 4 to the Company's Report on Form 10-Q for the thirty-nine weeks ended September 27, 1996.)
	Pursuant to Item 601(b)(4)(iii) of Regulation S-K, copies of certain instruments defining the rights of holders of certain long-term debt of the Company and its subsidiaries are not filed as exhibits because the amount of debt authorized under any such instrument does not exceed 10 percent of the total assets of the Company and its subsidiaries. The Company agrees to furnish copies thereof to the Securities and Exchange Commission upon request.
4.3	Rights Agreement dated as of March 9, 1990, between the Company and Norwest Bank Minnesota, National Association, as Rights Agent, including as Exhibit A the form of the Certificate of Designation, Preferences and Rights of Series A Junior Participating Preferred Shares. (Incorporated by reference to Exhibit 1 to the Company's Report on Form 8-K dated March 19, 1990.)
*10.1	1996 Corporate and Business Unit Annual Bonus Plan. (Incorporated by reference to Exhibit 10.1 to the Company's Report on Form 10-Q for the twenty-six weeks ended June 28, 1996.)
*10.2	Deferred Compensation Plan Restated, effective December 1, 1992. (Incorporated by reference to Exhibit 2 to the Company's Report on Form 8-K dated March 11, 1993.)
*10.3	Executive Deferred Compensation Agreement. Form of supplementary agreement entered into by the Company which provides a retirement benefit to executive officers, as amended by Amendment 1, effective September 1, 1990. (Incorporated by reference to Exhibit 3 to the Company's Report on Form 8-K dated March 11, 1993.)
*10.4	Chairman's Award Plan. (Incorporated by reference to Exhibit 3 to the Company's Report on Form 8-K dated March 7, 1988.)

*10.5	Executive Long Term Incentive Agreements. Form of restricted stock award agreement used for awards to executive officers. (Incorporated by reference to Attachment B to Item 5 to the Company's Report on Form 10-Q for the thirteen weeks ended March 29, 1991.) Form of restricted stock award agreement used for awards to Chairman. (Incorporated by reference to Attachment A to Item 5 to the Company's Report on Form 10-Q for the twenty-six weeks ended June 28, 1991.)
*10.6	Executive Long Term Incentive Agreement. Form of agreement used for restricted stock awards to two new officers. (Incorporated by reference to Attachment B to Company's Report on Form 10-Q for the thirteen weeks ended March 27, 1992.)
*10.7	Executive Long Term Incentive Agreement. Form of agreement used for one year restricted stock award to one officer. (Incorporated by reference to Exhibit 2 to Company's Report on Form 10-Q for the twenty-six weeks ended June 25, 1993.)
*10.8	Long Term Stock Incentive Plan as amended. (Incorporated by reference to Exhibit 10.2 to the Company's Report on Form 10-Q for the twenty-six weeks ended June 28, 1996.)
*10.9	Retirement Plan for Non-Employee Directors. (Incorporated by reference to Attachment C to Item 5 to the Company's Report on Form 10-Q for the thirteen weeks ended March 29, 1991.)
*10.10	Deferred Compensation Plan for Non-Employee Directors. (Incorporated by reference to Exhibit 2 to the Company's Report on Form 8-K dated March 7, 1988.)
*10.11	Restoration Plan, restating Excess Benefit Plan, effective as of July 1, 1988. (Incorporated by reference to Exhibit 1 to the Company's Report on Form 10-Q for the thirteen weeks ended March 26, 1993.)
*10.12	Stock Option Agreement. Form of agreement used for incentive stock option/alternative stock appreciation right award to selected officers, dated February 25, 1993. (Incorporated by reference to Exhibit 10.14 to the Company's 1993 Annual Report on Form 10-K.)
*10.13	Stock Option Agreement. Form of agreement used for non-incentive stock option/alternative stock appreciation right award to selected officers, dated May 4, 1993. (Incorporated by reference to Exhibit 10.15 to the Company's 1993 Annual Report on Form 10-K.)
*10.14	Nonemployee Director Stock Plan (Incorporated by reference to Exhibit 10.1 to the Company's Report on Form 10-Q for the twenty-six weeks ended July 1, 1994.)
*10.15	Stock Option Agreement. Form of agreement used for award of non-incentive stock options to executive officers, dated May 2, 1994. (Incorporated by reference to Exhibit 10.3 to the Company's Report on Form 10-Q for the twenty-six weeks ended July 1, 1994.)
*10.16	Stock Option Agreement. Form of agreement used for award of non-incentive stock options to selected officers, dated December 15, 1994, December 27, 1994 and February 23, 1995. (Incorporated by reference to Exhibit 10.16 to the Company's 1994 Annual Report on Form 10-K.)
*10.17	Stock Option Agreement. Form of agreement used for award of non-incentive stock options to executive officers, dated March 1, 1995. (Incorporated by reference to Exhibit 10 to the Company's Report on Form 10-Q for the thirteen weeks ended March 31, 1995.)
*10.18	Stock Option Agreement. Form of agreement used for award of non-incentive stock option to one executive officer, dated December 15, 1995. (Incorporated by reference to Exhibit 10.18 to the Company's 1995 Annual Report on Form 10-K.)

*10.19	Stock Option Agreement. Form of agreement used for award of non-incentive stock options to executive officers, dated March 1, 1996. (Incorporated by reference to Exhibit 10.19 to the Company's 1995 Annual Report on Form 10-K.)
*10.20	Salary protection arrangement with one executive officer. (Incorporated by reference to Exhibit 10.20 to the Company's 1995 Annual Report on Form 10-K.)
*10.21	Form of salary protection arrangement between the Company and executive officers. (Incorporated by reference to Exhibit 10.21 the Company's 1995 Annual Report on form 10-K.)
*10.22	Nonemployee Director Stock Option Plan. (Incorporated by reference to Exhibit 10.3 to the Company's Report on Form 10-Q for the twenty-six weeks ended June 28, 1996.)
*10.23	Stock Option Agreement. Form of agreement used for award of nonstatutory stock options to nonemployee directors, dated May 7, 1996. (Incorporated by reference to Exhibit 10.4 to the Company's Report on Form 10-Q for the twenty-six weeks ended June 28, 1996.)
*10.24	Stock Option Agreement. Form of agreement used for award of non-incentive stock options to executive officers, dated February 28, 1997.
*10.25	Stock Option Agreement Amendment. Form of amendment, dated March 8, 1997, used to remove alternative stock appreciation right from incentive stock option agreement dated February 25, 1993, for selected officers.
*10.26	Stock Option Agreement Amendment. Form of amendment, dated March 8, 1997, used to remove alternative stock appreciation right from non-incentive stock option agreement dated May 4, 1993, for selected officers.
11	Statement of Computation of Earnings per share included herein on page 33.
21	Subsidiaries of the Registrant included herein on page 34.
23	Independent Auditor's Consent included herein on page 34.
24	Power of Attorney included herein on page 35.
27	Financial Data Schedule (EDGAR filing only).
99	Cautionary Statement Regarding Forward-Looking Statements.

*Management Contracts, Compensatory Plans or Arrangements.

Exhibit Number 11

Graco Inc. & Subsidiaries

Computation of Per Share Earnings

(In thousands, except per share amounts)	Years Ended December 27, 1996	December 29, 1995	December 30, 1994
PRIMARY			
Net earnings applicable to common stock:			
Net earnings	$36,169	$27,706	$15,326
Less dividends on preferred stock	--	61	74
	$36,169	$27,645	$15,252
Average number of common shares and common equivalent shares outstanding:			
Average number of common shares outstanding	17,229	17,214	17,309
Dilutive effect of stock options computed based on the treasury stock method using average market price	255	206	63
	17,484	17,420	17,372
Net earnings per common share and common equivalent share	$ 2.07	$ 1.59	$ .88
FULLY DILUTED			
Net earnings applicable to common stock:			
Net earnings	$36,169	$27,706	$15,326
Less dividends on preferred stock	--	61	74
	$36,169	$27,645	$15,252
Average number of common shares and common equivalent shares outstanding:			
Average number of common shares outstanding	17,229	17,214	17,309
Dilutive effect of stock options computed based on the treasury stock method using the year end market price, if higher than average market price	277	227	73
	17,506	17,441	17,382
Net earnings per common share and common equivalent share	$ 2.07	$ 1.59	$ .88

Exhibit 21

Subsidiaries of Graco Inc.

The following are subsidiaries of the Company:

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

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

The Registrant has additional subsidiaries, which considered in the aggregate as a single subsidiary, do not constitute a significant subsidiary.

Exhibit 23

Independent Auditors' Consent

We consent to the incorporation by reference in Registration Statement No. 333-17691 on Form S-8 (the Company's Long Term Stock Incentive Plan), in Registration Statement No. 333-17787 on Form S-8 (the Company's Employee Stock Purchase Plan), in Registration Statement No. 33-54205 on Form S-8 (the Company's Nonemployee Director Stock Plan) and in Registration Statement No. 333-03459 on Form S-8 (the Company's Nonemployee Director Stock Option Plan) of our report dated January 20, 1997, appearing in this Annual Report on Form 10-K of Graco Inc. for the year ended December 27, 1996.

Deloitte & Touche LLP
Minneapolis, Minnesota
March 17, 1997

Exhibit 24

Power of Attorney

Know all by these presents, that each person whose signature appears below hereby constitutes and appoints George Aristides or Mark W. Sheahan, that person's true and lawful attorney-in-fact and agent, with full power of substitution and resubstitution for that person and in that person's name, place and stead, in any and all capacities, to sign the Report on Form 10-K for the year ended December 27, 1996, of Graco Inc. (and any and all amendments thereto) and to file the same with the Securities and Exchange Commission, granting unto said attorney-in-fact and agent, full power and authority to do and perform each and every act and thing requisite or necessary to be done in and about the premises, as fully to all intents and purposes as that person might or could do in person, hereby ratifying and confirming all that said attorney-in-fact and agent, or his substitutes, may lawfully do or cause to be done by virtue hereof.

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

	Date
/s/G. ARISTIDES G. Aristides	February 14, 1997
/s/R. O. BAUKOL R. O. Baukol	February 14, 1997
/s/D. A. KOCH D. A. Koch	February 14, 1997
/s/R. D. MCFARLAND R. D. McFarland	February 14, 1997
/s/L. R. MITAU L. R. Mitau	February 14, 1997
/s/M. A.M. MORFITT M. A.M. Morfitt	February 14, 1997
/s/D. R. OLSETH D. R. Olseth	February 14, 1997
/s/C. M. OSBORNE C. M. Osborne	February 14, 1997
/s/W. G. VAN DYKE W. G. Van Dyke	February 14, 1997

Exhibit 10.24

STOCK OPTION AGREEMENT
(NON-ISO)

THIS AGREEMENT, made this _____ day of ______________, 199__, by and between Graco Inc., a Minnesota corporation (the "Company") and (the "Employee").

WITNESSETH THAT:

WHEREAS, the Company pursuant to it's Long-Term Incentive Stock Plan wishes to grant this stock option to Employee;

NOW THEREFORE, in consideration of the premises and of the mutual covenants herein contained, the parties hereto hereby agree as follows:

1. Grant of Option

The Company hereby grants to Employee, the right and option (hereinafter called the "option") to purchase all or any part of an aggregate of Common Shares, par value $1.00 per share, at the price of $ per share on the terms and conditions set forth herein.

2. Duration and Exercisability

A. This option may not be exercised by Employee until the expiration of two (2) years from the date of grant, and this option shall in all events terminate ten (10) years after the date of grant. During the first two years from the date of grant of this option, no portion of this option may be exercised. Thereafter this option shall become exercisable in four cumulative installments of 25% as follows:

Date	Total Portion of Option Which is Exercisable
Two Years after Date of Grant	25%
Three Years after Date of Grant	50%
Four Years after Date of Grant	75%
Five Years after Date of Grant	100%

In the event that Employee does not purchase in any one year the full number of shares of Common Stock of the Company to which he/she is entitled under this option, he/she may, subject to the terms and conditions of Section 3 hereof, purchase such shares of Common Stock in any subsequent year during the term of this option.

B. During the lifetime of the Employee, the option shall be exercisable only by him/her and shall not be assignable or transferable by him/her otherwise than by will or the laws of descent and distribution.

3. Effect of Termination of Employment

A. In the event that Employee shall cease to be employed by the Company or its subsidiaries for any reason other than his/her gross and willful misconduct, death, retirement (as defined in Section 3(d) below), or disability (as defined in Section 3(d) below), Employee shall have the right to exercise the option at any time within one month after such termination of employment to the extent of the full number of shares he/she was entitled to purchase under the option on the date of termination, subject to the condition that no option shall be exercisable after the expiration of the term of the option.

B. In the event that Employee shall cease to be employed by the Company or its subsidiaries by reason of his/her gross and willful misconduct during the course of his/her employment, including but not limited to wrongful appropriation of Company funds or the commission of a felony, the option shall be terminated as of the date of the misconduct.

C. If the Employee shall die while in the employ of the Company or a subsidiary or within one month after termination of employment for any reason other than gross and willful misconduct and shall not have fully exercised the option, all remaining shares shall become immediately exercisable and such option may be exercised at any time within twelve months after his/her death by the executors or administrators of the Employee or by any person or persons to whom the option is transferred by will or the applicable laws of descent and distribution, and subject to the condition that no option shall be exercisable after the expiration of the term of the option.

D. If the Employee's termination of employment is due to retirement (either after attaining age 55 with 10 years of service, or attaining age 65, or due to disability within the meaning of the provisions of the Graco Long-Term Disability Plan), all remaining shares shall become immediately exercisable and the option may be exercised by the Employee at any time within three years of the employee's retirement, or in the event of the death of the Employee within the three-year period after retirement, the option may be exercised at any time within twelve months after his/her death by the executors or administrators of the Employee or by any person or persons to whom the option is transferred by will or the applicable laws of descent and distribution, to the extent of the full number of shares he/she was entitled to purchase under the option on the date of death, and subject to the condition that no option shall be exercisable after the expiration of the term of the option.

4. Manner of Exercise

A. The option can be exercised only by Employee or other proper party within the option period delivering written notice to the Company at its principal office in Minneapolis, Minnesota, stating the number of shares as to which the option is being exercised and, except as provided in Section 4(c), accompanied by payment-in-full of the option price for all shares designated in the notice.

B. The Employee may, at Employee's election, pay the option price either by check (bank check, certified check, or personal check) or by delivering to the Company for cancellation Common Shares of the Company with a fair market value equal to the option price. For these purposes, the fair market value of the Company's Common Shares shall be the closing price of the Common Shares on the date of exercise on the New York Stock Exchange (the "NYSE") or on the principal national securities exchange on which the shares are traded if the shares are not then traded on the NYSE. If there is not a quotation available for such day, then the closing price on the next preceding day for which such a quotation exists shall be determinative of fair market value. If the shares are not then traded on an exchange, the fair market value shall be the average of the closing bid and asked prices of the Common Shares as reported by the National Association of Securities Dealers Automated Quotation System. If the Common Shares are not then traded on NASDAQ or on an exchange, then the fair market value shall be determined in such manner as the Company shall deem reasonable.

C. The Employee may, with the consent of the Company, pay the option price by arranging for the immediate sale of some or all of the shares issued upon exercise of the option by a securities dealer and the payment to the Company by the securities dealer of the option exercise price.

5. Payment of Withholding Taxes

Upon exercise of any portion of this option, Employee shall pay to the Company an amount sufficient to satisfy any federal, state, or local withholding tax requirements which arise as a result of the exercise of the option or provide the Company with satisfactory indemnification for such payment.

6. Change of Control

A. Notwithstanding Section 2(a) hereof, the entire option shall become immediately and fully exercisable on the day following a "Change of Control" and shall remain fully exercisable until either exercised or expiring by its terms. A "Change of Control" means:

(1) acquisition by any individual, entity, or group (within the meaning of Section 13(d)(3) or 14(d)(2) of the Exchange Act of 1934), (a "Person"), of beneficial ownership (within the meaning of Rule 13d-3 under the 1934 Act) which results in the beneficial ownership by such Person of 25% or more of either

(a) the then outstanding shares of Common Stock of the Company (the "Outstanding Company Common Stock") or

(b) the combined voting power of the then outstanding voting securities of the Company entitled to vote generally in the election of directors (the "Outstanding Company Voting Securities");

provided, however, that the following acquisitions will not result in a Change of Control:

(i) an acquisition directly from the Company,

(ii) an acquisition by the Company,

(iii) an acquisition by an employee benefit plan (or related trust) sponsored or maintained by the Company or any corporation controlled by the Company,

(iv) an acquisition by any Person who is deemed to have beneficial ownership of the Company common stock or other Company voting securities owned by the Trust Under the Will of Clarissa L. Gray ("Trust Person"), provided that such acquisition does not result in the beneficial ownership by such Person of 32% or more of either the Outstanding Company Common Stock or the Outstanding Company Voting Securities, and provided further that for purposes of this Section 6, a Trust Person shall not be deemed to have beneficial ownership of the Company common stock or other Company voting securities owned by The Graco Foundation or any employee benefit plan of the Company, including, without limitations, the Graco Employee Retirement Plan and the Graco Employee Stock Ownership Plan,

(v) an acquisition by the Employee or any group that includes the Employee, or

(vi) an acquisition by any corporation pursuant to a transaction that complies with clauses (a), (b), and (c) of subsection (4) below; and

provided, further, that if any Person's beneficial ownership of the Outstanding Company Common Stock or Outstanding Company Voting Securities is 25% or more as a result of a transaction described in clause (i) or (ii) above, and such Person subsequently acquires beneficial ownership of additional Outstanding Company Common Stock or Outstanding Company Voting Securities as a result of a transaction other than that described in clause (i) or (ii) above, such subsequent acquisition will be treated as an acquisition that causes such Person to own 25% or more of the Outstanding Company Common Stock or Outstanding Company Voting Securities and be deemed a Change of Control; and provided further, that in the event any acquisition or other transaction occurs which results in the beneficial ownership of 32% or more of either the Outstanding Company Common Stock or the Outstanding Company Voting Securities by any Trust Person, the Incumbent Board may by majority vote increase the threshold beneficial ownership percentage to a percentage above 32% for any Trust Person; or

(2) Individuals who, as of the date hereof, constitute the Board of Directors of the Company (the "Incumbent Board") cease for any reason to constitute at least a majority of said Board; provided, however, that any individual becoming a director subsequent to the date hereof whose election, or nomination for election by the Company's shareholders, was approved by a vote of at least a majority of the directors then comprising the Incumbent Board will be considered as though such individual were a member of the Incumbent Board, but excluding, for this purpose, any such individual whose initial membership on the Board occurs as a result of an actual or threatened election contest with respect to the election or removal of directors or other actual or threatened solicitation of proxies or consents by or on behalf of a Person other than the Board; or

(3) The commencement or announcement of an intention to make a tender offer or exchange offer, the consummation of which would result in the beneficial ownership by a Person of 25% or more of the Outstanding Company Common Stock or Outstanding Company Voting Securities; or

(4) The approval by the shareholders of the Company of a reorganization, merger, consolidation, or statutory exchange of Outstanding Company Common Stock or Outstanding Company Voting Securities or sale or other disposition of all or substantially all of the assets of the Company ("Business Combination") or, if consummation of such Business Combination is subject, at the time of such approval by stockholders, to the consent of any government or governmental agency, the obtaining of such consent (either explicitly or implicitly by consummation) excluding, however, such a Business combination pursuant to which

(a) all or substantially all of the individuals and entities who were the beneficial owners of the Outstanding Company Common Stock or Outstanding Company Voting Securities immediately prior to such Business Combination beneficially own, directly or indirectly, more than 80% of, respectively, the then outstanding shares of common stock and the combined voting power of the then outstanding voting securities entitled to vote generally in the election of directors, as the case may be, of the corporation resulting from such Business Combination (including, without limitation, a corporation that as a result of such transaction owns the Company or all or substantially all of the Company's assets either directly or through one or more subsidiaries) in substantially the same proportions as their ownership, immediately prior to such Business Combination of the Outstanding Company Common Stock or Outstanding Company Voting Securities,

(b) no Person [excluding any employee benefit plan (or related trust) of the Company or such corporation resulting from such Business Combination] beneficially owns, directly or indirectly, 25% or more of the then outstanding shares of common stock of the corporation resulting from such Business Combination or the combined voting power of the then outstanding voting securities of such corporation except to the extent that such ownership existed prior to the Business Combination, and

(c) at least a majority of the members of the board of directors of the corporation resulting from such

Business Combination were members of the Incumbent Board at the time of the execution of the initial agreement, or of the action of the Board, providing for such Business Combination; or

(5) approval by the stockholders of the Company of a complete liquidation or dissolution of the Company.

B. A Change of Control shall not be deemed to have occurred with respect to an Employee if:

(1) the acquisition of the 25% or greater interest referred to in subparagraph A.(1) of this Section 6 is by a group, acting in concert, that includes the Employee or

(2) if at least 25% of the then outstanding common stock or combined voting power of the then outstanding company voting securities (or voting equity interests) of the surviving corporation or of any corporation (or other entity) acquiring all or substantially all of the assets of the Company shall be beneficially owned, directly or indirectly, immediately after a reorganization, merger, consolidation, statutory share exchange, disposition of assets, liquidation or dissolution referred to in subparagraph (c) or (d) of this definition by a group, acting in concert, that includes that Employee.

7. Adjustments

If Employee exercises all or any portion of the option subsequent to any change in the number or character of the Common Shares of the Company (through merger, consolidation, reorganization, recapitalization, stock dividend, or otherwise), Employee shall then receive for the aggregate price paid by him/her on such exercise of the option, the number and type of securities or other consideration which he/she would have received if such option had been exercised prior to the event changing the number or character of outstanding shares.

8. Miscellaneous

A. This option is issued pursuant to the Company's Long-Term Incentive Stock Plan and is subject to its terms. A copy of the Plan has been given to the Employee. The terms of the Plan are also available for inspection during business hours at the principal offices of the company.

B. This Agreement shall not confer on Employee any right with respect to continuance of employment by the Company or any of its subsidiaries, nor will it interfere in any way with the right of the Company to terminate such employment at any time. Employee shall have none of the rights of a shareholder with respect to shares subject to this option until such shares shall have been issued to him upon exercise of this option.

C. The Company shall at all times during the term of the option reserve and keep available such number of shares as will be sufficient to satisfy the requirements of this Agreement.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed on the day and year first above written.

GRACO INC.

____
By
Its:

____
Employee

Exhibit 10.25

AMENDMENT TO
STOCK OPTION AGREEMENT
(ISO/ALTERNATIVE SAR)

This Agreement made this ______ day of March, 1997, by and between Graco Inc., a Minnesota corporation (the "Company") and _________________________ (the "Employee").

WHEREAS, the Employee and the Company entered into a Stock Option Agreement (ISO/Alternative SAR), on the 25th day of February, 1993, (the "Option Agreement")which contains provisions permitting the Employee to exercise stock appreciation rights as an alternative to the stock options granted by the Option Agreement to the Employee under the Graco Inc. Long Term Stock Incentive Plan;

WHEREAS, the parties to the Option Agreement wish to remove the provisions relating to alternative stock appreciation rights from the Option Agreement;

NOW, THEREFORE, the parties hereby mutually agree, for good and valuable consideration, which is hereby acknowledged, to amend the Option Agreement by deleting the words enclosed in quotation marks and the identified sections from both agreements as follows:

1. "/Alternative SAR" from the title;

2. "and an alternative SAR" from the first WHEREAS clause;

3. Section 1(c) in its entirety; and

4. Section 4 in its entirety.

IN WITNESS WHEREOF, the parties have caused this Amendment Agreement to be executed as of the day and year first above written.

GRACO INC.

____
By
Its:

____
Employee

Exhibit 10.26

STOCK OPTION AGREEMENT
(NON-ISO/ALTERNATIVE SAR)

This Agreement made this _____ day of March, 1997, by and between Graco Inc., a Minnesota corporation (the "Company") and (the "Employee").

WHEREAS, the Employee and the Company entered into a Stock Option Agreement (NON-ISO/Alternative SAR) on the 4th day of May, 1993, (the "Option Agreement") which contains provisions permitting the Employee to exercise stock appreciation rights as an alternative to the stock options granted by the Option Agreement to the Employee under the Graco Inc. Long Term Stock Incentive Plan;

WHEREAS, the parties to the Option Agreement wish to remove the provisions relating to alternative stock appreciation rights from the Option Agreement;

NOW, THEREFORE, the parties hereby mutually agree, for good and valuable consideration, which is hereby acknowledged, to amend the Option Agreement by deleting the words enclosed in quotation marks and the identified sections from the Option Agreement as follows:

1. "/Alternative SAR" from the title;

2. "and an alternative SAR" from the first WHEREAS clause;

3. Section 1(c) in its entirety; and

4. Section 4 in its entirety.

IN WITNESS WHEREOF, the parties have caused this Amended Agreement to be executed as of the day and year first above written.

GRACO INC.

____
By
Its:

____
Employee

Exhibit 99

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

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

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

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

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

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

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

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

- The prospects and operating results of the Company's Industrial Equipment Division may be affected by the capital equipment spending levels of industrial customers, the availability and cost of financing, changes in the environmental regulation of coatings, and the ability of the Company to meet changing customer requirements.

- The prospects and operating results of the Company's Lubrication Equipment Division may be affected by variations in the equipment spending levels of the major oil companies, and the relative market strength and pricing strategies of competitors, especially in major foreign markets.

- The prospects and operating results of the Company's Automotive Equipment Division may be affected by the equipment purchase plans of major automobile manufacturers worldwide (which are in turn impacted by the level of automotive sales worldwide), changes in automotive manufacturing processes, and the pricing strategies of competitors.

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THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM GRACO INC. AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF EARNINGS AND CONSOLIDATED BALANCE SHEETS FOR THE 52 WEEKS ENDED DECEMBER 27, 1996 AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS.

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

12-MOS
DEC-27-1996
DEC-30-1995
DEC-27-1996
1
6,535
0
83,474
4,700
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247,814
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36,169
2.07
2.07